



REPORT

Condition for Success 2: “Financing Water for All”

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The views and opinions expressed in this report are those of the authors and do not necessarily reflect the position of the International Forum Committee or its member organisations.

1. Introduction

This paper has been developed as a background paper for the Conditions for Success 2 “Financing Water for All” (CS2) identified by the thematic process commission of the Sixth World Water Forum. The latter, defined as “the forum of solutions” will take place in Marseille between 12th and 17th March 2012. In advance of the Forum, a core group of leading sector institutions has been assembled to set ambitious but yet achievable targets for the sector with respect to financing water for all and identify solutions to achieve such targets. The present background paper presents an overview of this work, based on the papers prepared by each of the seven Target and Solutions Groups (TSGs) formed under CS2.

Ensuring that sufficient financing is mobilised in order to reach ambitious targets and objectives for the water sector is absolutely critical. In many countries, the investments needed to deliver sustainable water and sanitation services, expand their coverage and upgrade service delivery to meet current social and environmental expectations, are huge. Throughout the world, the challenges of providing access to safe water and sanitation are further accentuated by increasing demands from other water uses due to factors such as population increase, pressures to increase food production, rapid urbanisation, degradation of water quality, and increasing uncertainty about water availability in the context of climate change.

Addressing these challenges will require both large capital investments for new or upgraded infrastructure, on-going investments in operations and maintenance and funding of critical “soft” activities, such as governance reforms or capacity building.

The benefits from such investments for society are substantial. Yet, most systems are underfunded with dire consequences for water and sanitation users, especially the poorest. Underfunding also has profound impacts agricultural productivity as well as for the sustainability of water resources and the environment, and thus, the services that it provides. Providing sustainable drinking water supply and sanitation services and other water needs requires a sound financial basis and strategic financial planning to ensure that existing and future financial resources are commensurate with investment needs as well as the costs of operating and maintaining services.

Providing adequate financing is therefore a necessary condition for success for improving water resource management and the delivery of water and sanitation services, although by no means a sufficient one.

This paper is structured as follows:

- **Section 2** provides some background on “water financing” as an issue (and how it has evolved over the years) and identifies where key challenges lie;
- **Section 3** sets out the targets and the solutions identified and proposed by this group to tackle some of these challenges;
- **Section 4** identifies the remaining challenges requiring different and complementary initiatives;
- **Section 5** sets out a concrete plan of key commitments and monitoring arrangements for implementing the proposed solutions beyond 2012;
- **Section 6** concludes with key messages coming out of this exercise.

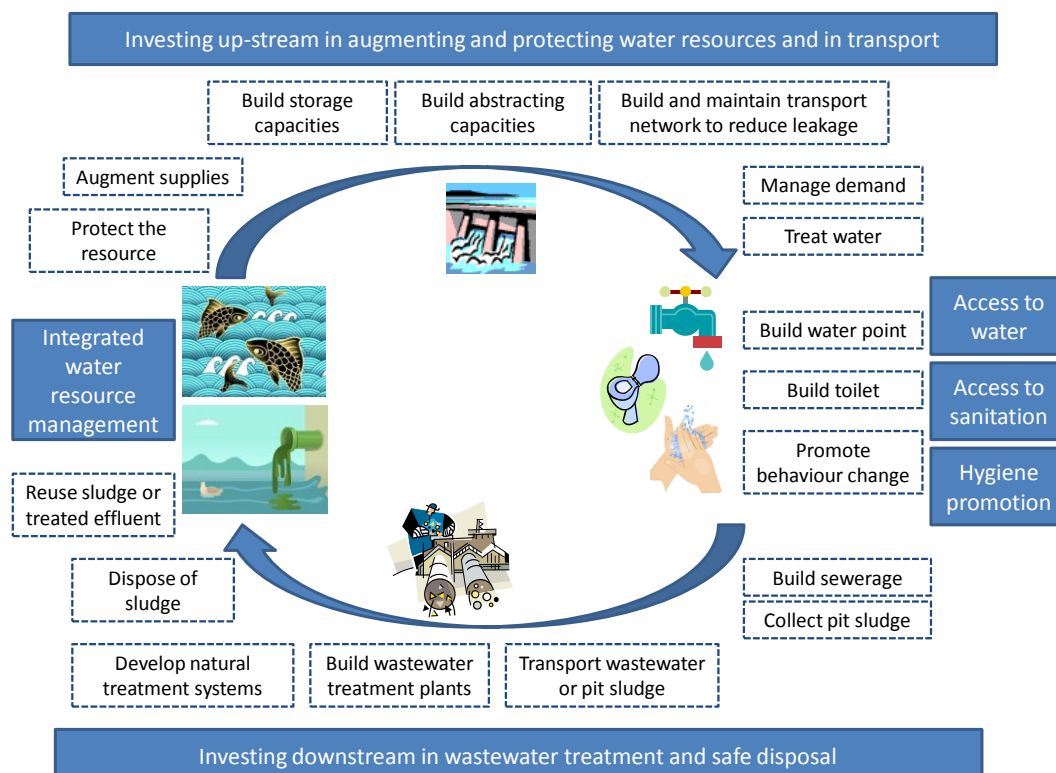
2. Background and rationale

This section sets out the rationale for considering financing as a condition for success of any initiative to guarantee the sustainable management of water resources and improve the delivery of water, sanitation and irrigation services.

Why does the water sector needs financing?

Even though water “falls from the sky”, processing water from the point where it is collected to the point where it is used and/or discharged into the environment (treated or untreated) is expensive, requiring appropriate infrastructure to be built and managed sustainably over time. The types of investments that are required to deliver those services are schematically represented in Figure 1.

> **Figure 1. The value chain of sustainable water and sanitation services**



Source: OECD (2010).

This Figure shows that, at each step of the value chain, investments in a whole range of “water services” need to be made, ranging from protecting the raw material (freshwater resources) to building storage capacity or water transport networks, all the way to investments into collection, safe disposal, treatment or re-use of wastewater. Once built, the infrastructure should be adequately maintained and operated so as to provide sustainable, affordable and reliable access to water and sanitation services to all. New and recurrent investments in water and sanitation services are critical in order to expand access to the services and maintain their ability to deliver benefits overtime. The same concept applies to irrigation infrastructure for agricultural

productivity. Overall, investments are needed to maintain the integrity of the water resources and the sustainability of the environment and the services it provides.

Financing needs are particularly acute in developing and transition countries. According to the WHO 2010 Update on the Progress of Sanitation and Drinking Water (WHO/UNICEF 2010), 2.6 billion people, or one third of the world's population, do not use improved sanitation facilities and 884 million people still lack access to improved sources of water (almost all of them live in developing countries). The poorest people in these countries are those that suffer most. For example, in Sub-Saharan Africa, 77% of the richest quintile of the population has access to improved sanitation facilities and only 4% practice open defecation. In the poorest quintile, only 16 % have improved sanitation facilities and 63% practice open defecation. The distribution for access to water is similar: while 35% of the richest quintile has in-plot piped water and 51% have access to other improved sources, only 36% of the poorest quintile use improved sources and less than 1% have in-plot piped water.

How have water investments been financed in the past?

Looking back at how water investments have been financed in the past can give us clues as to what solutions could be defined in future. Mobilizing adequate financing for building and operating water infrastructure has been a key preoccupation of human societies for millennia, since the development of agriculture and irrigation (which was key to the development of ancient civilizations) and the establishment of cities, which required providing water at fixed points on a reliable basis and removing wastewater and faecal sludge to prevent epidemics. In ancient civilizations, political leaders would often build large-scale “pharaonic” projects for irrigation or serving their palace's gardens and fountains, in order to demonstrate their power and ingenuity. In the meantime, ordinary people in rural communities and towns were often left to fend off for themselves, relying on local water sources.

The Roman Empire was the first one to build large and complex infrastructure to serve urban needs (including aqueducts and sewerage networks). This supported the establishment and growth of its Imperial capital, Rome, which at its peak reached 1 million people, a figure never heard of previously for an urban centre. Building imposing aqueducts throughout the Empire was usually the remit of the army, as a way of keeping soldiers fit and healthy and spreading Roman civilisation (and, in particular, its obsession with bathing and cleanliness). Once built, the aqueducts would serve all classes, either in patricians' homes on a paying basis or via a network of public basins and fountains for the ordinary people. Whilst the State and, in some cases, rich private individuals (such as Marcus Agrippa, aedile of Rome) took care of capital expenditure, they relied on a mix of financing sources to cover operating costs!



*Legend: Roman Aqueducts (The Pont du Gard) and sewers (section of the famous “Cloaca Maxima” in Rome).
Source: see Steven Solomon (2010) for more detail on the Roman Empire's water systems.*

As the Roman Empire went into gradual decline and subsequent collapse, its water infrastructure got increasingly degraded. When the Barbarians reached the gates of Rome, one of their primary targets was to destroy its aqueducts, thereby disrupting all the water distribution channels, sewers or even waterwheels used for bread production.

Following the demise of the Roman Empire, it would take several hundred years before water and sewerage networks would once again serve large portions of urban populations. In medieval times, the City of London for example started to build water networks using pipes of clay, sandstone, lead and hollowed-out elm trees. According to Halliday (2009), the water was freely available to householders but from 1312, revenue was collected to maintain and repair the pipes. Given the inability of public institutions to meet the rapidly expanding urban populations, small-scale providers including water carriers, night soil handlers, etc. emerged to fill the gap. These were entirely privately financed and in some cases highly organised (London saw the formation of a water-carriers association as early as 1496, with the creation of “The Brotherhood of St Cristofer of the Waterbearers”).

Over the years, a number of private projects and companies emerged to serve rapidly expanding cities, particularly from the mid-19th century. In France, the Compagnie Générale des Eaux was created in 1853 to supply drinking water to cities and irrigation services in the countryside. They signed the first ever concession contract for drinking water supply with the city of Lyon in 1853, for 20 years at a fixed price. The Lisbon water utility was itself private for decades before being nationalised in 1974. Private sector management was in several cases combined with public sector financing. For example, in France, a national fund for extending water services in rural areas (Fonds National pour le Développement des Adductions d’Eau Potable, FNDAE) was created in 1954 to finance the extension of coverage in rural areas whilst at the same time, the three leading private companies in the country were gaining market share by signing PPP contracts with cities, towns as well as small rural communities.

The need to combine several sources of funding, from households, governments and private financiers has therefore been around for a long time, with each country having to define the most appropriate mix of financing sources depending on their political priorities, institutional set-up and financing needs. More recently, an international debate has emerged on water sector financing issues, with a view to defining broad guidance for addressing those issues.

The emergence of “water financing” as an area for international debate

The emergence of an articulated discourse at the international level on the “water sector financing” issue is relatively recent.¹ The International Decade for Water and Sanitation, which ran from 1990 to 2000, focused on technical fixes and subsidised public investments. Despite important efforts, the objective of bringing universal access to water was not achieved. The first World Water Forum held in Marrakech (1997), as well as the second one in The Hague (2000) did not refer to “financing” as a specific issue: they were more focused on addressing the physical and technical challenges relating to the preservation and adequate distribution of water resources, particularly between types of water uses or across trans-boundary lines. At that time, in the late 1990s, the debate on the management of water services was polarized between the supporters of private sector participation (PSP), who saw PSP as a key way to bring fresh financing to the sector and the opponents of PSP, who considered that water is a natural resource and could not be the object of a commercial transaction.

¹ See a timeline of water-related events prepared by UNESCO [here](#): “1972 to 2006: from Stockholm to Mexico”.

Financing water started emerging as a key area for international debate at the start of the 21st century. The adoption of the Millennium Development Goals for water in 2000 and for sanitation at the World Summit on Sustainable Development (or Earth Summit) held in Johannesburg in 2002, contributed to placing renewed emphasis on financing for the sector, both at the international and at the national levels. As soon as State leaders had committed to reaching ambitious targets in terms of expanding access to water and sanitation services, it became necessary to evaluate the costs of achieving these targets, identify where financing resources would come from and understand whether mobilising additional resources might be required. This process started taking place at the international level (for example, through the efforts of the European Union Water Initiative Finance Working Group, created in 2002) and at the domestic level, led by national governments.

The “financing theme” came to the fore at the 2003 World Water Forum in Kyoto, which had elected to make financing one of the major themes for the Forum as a whole. The Panel on Infrastructure Financing (referred to as the “Camdessus Panel”) was formed in late 2001 “to address the ways and means of attracting new financial resources to the water field”. The Panel produced a report that neatly captured and distilled state-of-the-art sector knowledge and ideas in this area, including with respect to the adoption of innovative financing mechanisms for the sector.² One of their key recommendations was to double financial flows to the sector. The report advised that most of its recommendations be implemented by 2006 and that 2015 should be the next essential check-point, opening the third stage of a strategy leading to universal access to water and sanitation by 2025.

Financing was also a key theme of the subsequent World Water Fora. The Gurría report, published in the context of the 4th World Water Forum in Mexico in 2006, took as its main focus the demand for finance and the scope for developing the financial capacity of sub-national entities.³ The Gurría Report also included financing water for agriculture, recognizing the importance of significant underinvestment and cost recovery in this sector. Concern for agriculture water financing will continue to grow as food security issues loom large on the horizon.

In the 5th World Water Forum in Istanbul, in 2009, the OECD played a leading role on the financing theme, with a number of key publications clarifying concepts and defining a harmonised terminology for costs and financing sources (the “3Ts”). A key recommendation was to mobilise financing from a combination of sources rather than being solely focused on raising funding via tariffs, as explained below in more detail. The Istanbul Ministerial Statement promoted realistic and sustainable financing strategies for the water sector and recognition of the sustainable cost recovery principles (see Box 1 extracts below concerning financing).

² Winpenny, J. (2003).

³ Van Hofwegen, Paul. (2006).

> **Box 1 – Istanbul Ministerial Statement (2009)– extracts relative to financing**

18. We strive to **prioritize water and sanitation in national development plans and strategies**; develop local and national/regional water management plans; allocate adequate budgetary resources to water management and sanitation service provision; to lead donor coordination processes, and create an enabling environment for water and sanitation investments. **We strive to mobilize resources from all sources, including public and private.**

19. **We will promote effective use of financial resources from all sources**, including international financial institutions, development partners and beneficiary countries to increase support for water management, water supply and sanitation. We also will resolve to support more effective and diversified support, credit and financial management systems that are easily accessible and affordable.

20. Acknowledging that new and adequate resources are needed to achieve the MDGs, **we call upon the international community, development partners and private sources of financing to invest resources to complement the efforts made by developing countries and countries with economies in transition**, to develop sustainable water resources management and to build the infrastructure base for a sustained socio-economic growth, especially in Africa and least developed countries.

21. **We acknowledge the need for fair, equitable and sustainable cost recovery strategies and we will therefore promote and implement realistic and sustainable financing strategies for the water sector**, especially water supply, good water quality and sanitation sectors. We acknowledge that exclusively economic approaches and tools cannot capture all social and environmental aspects in cost recovery. Financing strategies should be based on a best possible use and mix of tariffs for all forms of water services, taxes and transfers to cover needs related to infrastructure development and extension, operation and maintenance.

Source: 5th World Water Forum Ministerial Process, Ministerial Statement

One constant preoccupation has been to try and raise the profile of the “water financing”, so as to reach Finance Ministers who make resource allocation decisions across sectors. To achieve this goal, the Sanitation and Water for All initiative held the first High Level Meeting in 2011 bringing together Ministries of Finance of donor and recipient governments to raise the profile of the water financing issue. The objective of this meeting (held alongside the World Bank and IMF meetings) is to convince Finance Ministers in developed and developing countries that the water sector is worth investing in. A number of governments have committed to increasing their sectoral allocation following such meetings but it is still too early to tell at this stage whether these commitments will be followed by actual investments.

How can the costs of providing water services be covered?

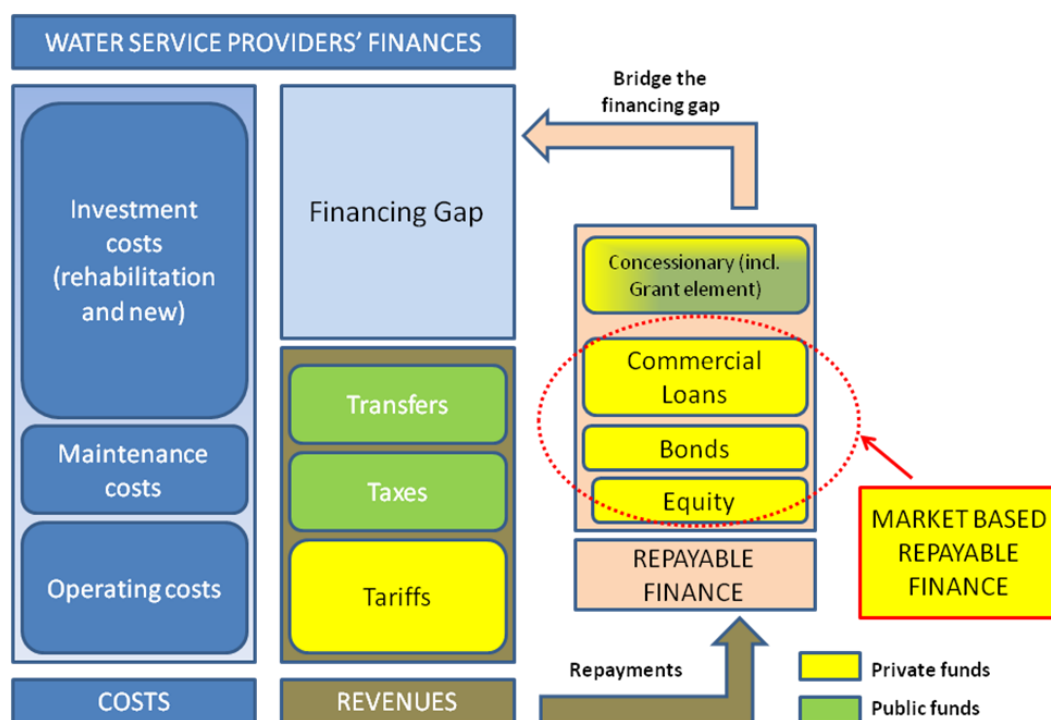
To better understand the debate on water sector financing, it is essential to clarify a number of key concepts with respect to what needs to be financed and how it can be financed. In most economic sectors, investment and recurrent costs need to be covered by matching financing so as to ensure that service providers do not go bankrupt. The public nature of water and sanitation service provision does not allow its providers to go bankrupt but tends to maintain utilities in a permanent underfunding situation, constraining the capacity to extend the services to all the population, impacting negatively on the quality of the services, and leading to a continuous degradation of the assets and inefficiency of the systems.

During the 1990s, it was commonly prescribed that tariffs from end-users of water services should cover all the costs, so that “water” would in effect “pay for water”. In practice, however, achieving full-cost recovery (FCR) from tariffs is often difficult in the water sector, due to the

scale of the required investments, the fact that many of these investments benefit a broader public than those who can be charged for the service (including future generations) and that the poor need equal access to the services when they may not be able to afford high tariffs. In the agricultural sector, full cost recovery is also made difficult by the fact that many countries provide free or cheap water to farmers as an explicit strategy to ensure cheap food and food self-sufficiency.

The OECD (and other international institutions) argues that such costs should be covered by a combination of sources, including tariffs, taxes and transfers, referred to collectively as “the 3Ts”. These three sources represent the “bedrock” of WASH services financing and the basis for “sustainable cost recovery” (SCR). SCR entails securing future cash flows from a combination of the 3Ts, and using this revenue stream as the basis for attracting **repayable sources of finance** such as loans, bonds and equity (depending on the local situation). As water and sanitation investments are typically substantial and lumpy, mobilising repayable finance may be needed to bridge a temporary financing gap and help smooth out the burden of these investments over a longer period (see Figure 2 below).

> **Figure 2 – Sources of finance for water and sanitation**



Source: OECD (2010a)

> Box 2 - Defining the 3Ts

Tariffs are funds contributed by users of WASH services for obtaining the services. Users generally make payments to service providers for getting access to the service and for using the service. A number of additional charges may be payable to the service provider, such as meter rental, penalty charges (for late payment or tampering with the meter), etc... In the event of cross-subsidies, tariffs paid by other user groups or users of other services (for example, users of electricity services when water and electricity services provision are combined) would be included in “tariffs”. Finally, when the service is self-provided (for example, when a household builds and operates their household latrine), the equity invested by the household (in form of cash, material or time - “sweat equity”) would also fall under “tariffs”.

Taxes refer to funds originating from domestic taxes which are channelled to the sector via transfers from all levels of government, including national, regional or local. Such funds would typically be provided as subsidies, for capital investment or operations. “Hidden” forms of subsidies may include tax rebates, soft loans (i.e. at a subsidised interest rate), transfers from local government housing taxes, donations, subsidised services (such as subsidised electricity) or “dormant” equity investments.

Transfers refer to funds from international donors and charitable foundations (including NGOs, decentralized cooperation or local civil society organizations) that typically come from sources external to the country, i.e. are contributed by tax payers or individual donors in other countries. These funds can be contributed either in the form of grants, concessionary loans (i.e. loans that include a “grant” element in the form of a subsidised interest rate or a grace period) or guarantees.⁴

Taken together, the 3Ts are the sources of funds that can allow sustainable financing of water services, either for the sector as a whole, a water utility or a decentralised government responsible for providing water, sanitation or irrigation services. As long as these sources are predictable over time, a water service can be financed by a combination of the 3Ts that will appear locally adequate. Some countries may choose to focus more on tariffs for cost-recovery, others will prefer to finance their water sector via taxes.

Estimating which costs need to be covered and how much financing is required to cover those costs are critical steps towards mobilising adequate financing. It is only if there is clarity on where funding from the 3Ts is going to come from that repayable financing can be leveraged, either from public or private sources. Reducing costs through efficiency gains can be an important first step for freeing up financial resources.

How has financing to the sector evolved in the last 10 years?

Over the last decade, financing flows to the sector have not doubled, despite the Camdessus Panel’s injunctions. Some of the financing flows to the sector have increased, such as international transfers. According to OECD (2011), after a temporary decline in the 1990s, aid to water and sanitation from international donors that report to the Development Assistance Committee (DAC) has been rising sharply since 2001. In 2008-09, total annual average aid commitments to water and sanitation amounted to USD 8.1 billion. Bilateral aid to water increased at an average annual rate of 18% over the period 2002-09 and multilateral aid also rose by 10% annually. During that period, the share of aid to water and sanitation in DAC members’ aid programmes also rose. In 2008-09, aid to water and sanitation represented 8% of DAC members’ bilateral sector-allocable aid.

⁴ Guarantees can be an effective way to use public funds (domestic and international) to attract repayable finance to the sector, as they would help with reducing interest rates and lengthening lending maturities. However, their use in the WASH sector remains limited, for reasons discussed in OECD (2010a).

Tracking other types of financing to the sector remains extremely difficult, however, particularly when the management of water services is decentralized. As a result, it is impossible to assess whether, as a global trend, funding to the sector from domestic taxes or from tariffs has increased or not. The first GLAAS report (Global Analysis and Assessment of Sanitation and Drinking Water) was published in 2010. The report sought to estimate how much spending has been allocated by domestic governments to the sector but found that it was remarkably little as a percentage of GDP. However, the GLAAS has identified that its methodology for collecting this type of data needed to be improved and will publish recommendations to that effect in the 2012 GLAAS report (see Section 3.2. for more detail).

What are the main issues that need to be addressed with respect to financing?

Mobilising investments for the sector is likely to continue to be difficult in the context of the global economic crisis. For that reason, it will be necessary to identify more efficient and smarter ways to deploy the limited funding available for the sector. The sector is currently facing a number of challenges in that respect, as summarised below.

There is an overall lack of transparency with respect to how much financing is currently allocated to the water sector, how much might be required and for what. Cases abound where overly ambitious plans to extend the coverage and level of WSS services need to be replaced by more realistic programmes, tailored to ensure financing for appropriate operation and maintenance, essential repairs and rehabilitation of critical elements of the WSS infrastructure, as well as sustainable extension where appropriate. In the absence of a large increase in overall funding allocations, an increased focus needs to be placed on reducing costs through efficiency gains, adjusting future expectations to match funding and mobilising additional sources through innovative financing.

The capacity to develop a strategic approach to financing of WSS in developing and transition countries needs to be strengthened. For instance, in the 1990s many countries in Eastern Europe, the Caucasus and Central Asia (EECCA) tried to develop target programmes for WSS infrastructure rehabilitation and development, but failed to implement them because data were lacking for robust policy analysis and policy making; priorities were neither clear, nor clearly linked to policy, investment projects were too many and too costly (unrealistic “wish lists”); expenditure needs much exceeded available finance; policy objectives were misaligned with institutional arrangements; and low management, financial and absorptive capacities created barriers for programme implementation.

Many investments in the sector have not yielded concrete results or been sustained because there has been an insufficient focus on accompanying software measures. This has been particularly the case for sanitation investments, for example, when “soft measures” for triggering demand or influencing behaviour change have not (or insufficiently) been funded. One key issue with planning and budgeting for soft measures is that there is very limited information about their costs and their effectiveness. Therefore, a key issue remains understanding, measuring, and monitoring the value of soft measures in the water and sanitation sector.

One of the biggest challenges relates to the sustainability of service delivery. Currently the focus is very clearly on one-off investment: governments and donors almost exclusively concern themselves with the capital expenditure costs of WASH services without taking account of the financial needs for operations and maintenance and post-construction maintenance. Although these costs should in theory be covered by user charges (or tariffs), those costs are frequently

under-estimated and several factors mean that tariffs are typically inadequate to cover costs, rarely exceeding O&M costs. Tariff collection remains very often insufficient and insufficient measures are taken to improve collection. Visibility regarding future income and revenue is limited, thereby limited the capacity to plan future investments and allocate funds to maintenance.

Available financing mechanisms are often not tailored to actual needs. Capital-intensive infrastructure needs long-term funding at affordable cost but this type of funding is difficult to secure, especially in the water sector which is perceived as high risks/ low returns, particularly in the current financial climate

Despite the OECD spear-heading a major effort for explaining key financing concepts to water sector professionals, **there are still a number of “enduring misconceptions” about financing of water and sanitation that need to be “debunked”, such as the following ideas:**

- That the sector should always be fully financed through tariffs (i.e. full cost recovery from tariffs) when in fact a mix of financing sources (the 3Ts) can be used to cover costs;
- That average tariffs must be kept low to ensure affordability for the poor. In reality, low tariffs do not benefit the poor when they are not connected to the network as connection charges are typically set high and prevent them from connecting. When the poor are connected, affordability is better achieved by introducing appropriate tariff structures with carefully targeted cross-subsidies or non-tariff support mechanisms;
- That governments (domestic governments and international donors) are the largest contributors of finance to the sector, when households themselves often are;
- That the private sector can “bring” substantial amounts of financing to the sector, when they can contribute to bridging a temporary finance gap but would ultimately need to be repaid.

Local stakeholders find it difficult to access the financial resources they need to develop water and sanitation services. Although decentralization is acknowledged as an important mean for fostering improved performance in the provision of water and sanitation, in many cases, the political and institutional framework for financial decentralisation is still incomplete. All local stakeholders (local authorities, local water utilities, small-scale private water providers, community water associations) need financing to increase access to services and maintain service quality.

Financing investment in agricultural water resources and irrigation has unique challenges. In most cases, irrigation water prices are significantly less than the costs of operating and maintaining the infrastructure and generally there has been no user contribution to capital costs. As noted, this is part of a conscious policy to promote food security through food self-sufficiency. As a result, it is very difficult to attract private financing unless there would be accompanying large public subsidies, which are also generally inadequate. In this situation, new and replacement investments are inadequately financed and infrastructure along with agricultural productivity declines in a downward spiral (Gurría, 2006). Attempts to reform this situation not only require financing but also larger institutional reforms to the irrigation, water resources management and agriculture sectors in which irrigation is embedded.

Financing of measures that enable sustainability of the services, such as protection of the water resources and promotion of water saving is insufficient. The underlying ecosystems are important for a range of economic activities and amenities. As a result, financing should be clearly allocated to help protect and restore ecosystems.

Finally, **identifying and implementing water and sanitation financing solutions that genuinely reach the poorest remains a key challenge in low-income countries worldwide**, in both rural and

urban contexts. As the poor are often left out of existing water and sanitation systems, particularly in developing countries, they pay a comparatively higher price for accessing inadequate services, whilst bearing the brunt of the costs associated with lack of service (through disease, malnutrition, reduced school attendance, decreased productivity, time lost...)

3. TSG's progresses: Target action plans, solutions and commitments

3.1. TSG's key progresses in tackling the main issues

This Core Group has identified targets and solutions to mobilise additional financing across all sub-components of the broad “water sector”, including for the provision of water, sanitation and irrigation services, the financing of software support services and that of the integrated management of water resources.

Strategic financial planning (SFP) (Target 1) is a process that decision-makers can use at national and regional level to define achievable targets and financially sound planning, taking into account limited public funding. SFP can help governments determine the overarching framework within which they can define a Sustainable Cost Recovery strategy (Target 3) to achieve an appropriate balance between the three main sources of revenues for the sector, which are commonly referred to as the 3Ts (Tariffs, Tax-based subsidies and Transfers from abroad) and meet current and future costs of investment, maintenance and operation).

This needs to be accompanied by “soft measures” and capacity building (Target 2) in order for local authorities and other service providers to ensure efficient service delivery (Target 4), by an understanding of the innovative sources of repayable financing for water service providers (Targets 5 and 7), measures to aid “pro-poor” financing (Target 7) and an understanding of the specific challenges raised by the need to finance agricultural water services and integrated water management (Target 6).

Table 1 below sets out the Targets as well as key milestones from the Target Action Plans.⁵ Summaries of each Target's rationale and proposed solutions appear below the Table, with a particular focus on the solutions presented by each group. The complete list of solutions proposed by each group and those that appeared on the Platform of Solutions is provided in the background paper and session plans for each target.

⁵ The detailed Target Action Plans are available in the individual session papers.



> Table 1. Conditions for Success 2 – Targets and Target Action Plan Overview

| Targets | Target Action Plan Overview | TSG Coordinator |
|---|---|--------------------|
| <p>Target 1: Strategic Financial Planning By 2015, a number of countries are aware of and have expressed support to the concept of Strategic Financial Planning for WSS and most of these countries have engaged in the process of developing a strategic plan or have set a clear timeline for when to do this.</p> | <ul style="list-style-type: none"> • Create before the end of 2012 a knowledge platform on strategic financial planning that will enable experience-sharing. • By 2014, all major International Financial Institutions and a number of countries have undertaken to include strategic financial planning as an integral part of the process of providing financial support to the WSS sector, consistent with the undertakings under Target CS2.2; • By 2015, further develop the strategic financial planning toolkit to make it accessible in a cost-effective manner for countries that are resource or data poor, as well as make it useful for local authorities. | OECD World Bank |
| <p>Target 2: Financing Soft Measures By 2015, a number of countries allocate an agreed percentage of the resources identified through strategic financial planning for “Soft measures” (capacity building, project preparation, etc.)</p> | <ul style="list-style-type: none"> • By end-2012, the relevant ministries and departments in both donor and pilot developing countries clearly identify and map their financial allocation to soft measures and to auditing and monitoring key programs in WSS. • In parallel, (an identified group of) donors and NGOs track soft measure spending and related outputs and outcomes in a systematic way (e.g. using a harmonized template). • By end-2012, a base line study is initiated to establish the current level of resource allocation on “essential soft measures”. • By end-2013, develop a guide to allocate resources to “essential soft measures” based on global “good practices”. • By 2015, develop a clear and tested methodology for identifying, documenting, and valuing soft measure benefits with a view to establish added value of the “essential soft measure”. • By 2015, a commitment is made by donors, NGOs and pilot countries to ensure that essential soft measures are adequately – and explicitly – financed. | WSP WEDC |

| Targets | Target Action Plan Overview | TSG Coordinator |
|---|--|--------------------|
| <p>Target 3: Sustainable cost recovery (SCR) that is financially sustainable, reliable and socially equitable</p> <p>By 2015, 10 countries, cities or providers (at least 2 per region) have inscribed in their water policies or statutes the achievement of sustainable cost recovery through a combination of Tariffs, Tax-based subsidies and Transfers from abroad (e.g. ODA, remittances) that is financially sustainable, reliable and socially equitable.</p> <p>This should be accompanied by a clear methodology to compute the costs that should be covered, a formula to determine tariff levels and a process for their periodic review, a choice of tariff structure, and mechanisms that ensure affordability for users. For those countries where tariff revenues do not fully recover costs, mechanisms should be in place that ensure revenue from tax-based subsidies and transfers that are adequate, reliable and predictable, to ensure that any combination of the 3Ts provide total revenues that cover all costs sustainably.</p> | <ul style="list-style-type: none"> • By 2012: a Glossary and toolkit with key definitions concerning Sustainable Cost Recovery is endorsed by representatives of national and local governments, public and private sector providers (or their associations), regulators, consumer groups and financial institutions (public, private, international). A group of stakeholders agree to work for its broadest possible diffusion and commits to work together to that effect. The Glossary is incorporated in the platform for SFP mentioned in Target CS2.1; • By 2014: all major International Financial Institutions and a number of countries have undertaken to include SCR as an integral part of the process of providing financial support to the WSS sector, consistent with the undertakings under Target 1 and 2 above; • By 2015: a SCR toolkit is prepared, in coordination with the SFP toolkit mentioned in Target CS2.1. | <p>EIB IWA</p> |
| <p>Target 4: Local-level financing</p> <p>By 2015, more than half of countries per region having transferred competence in the water and/or sanitation sector to the local authorities will have set up a financial mechanism allowing direct access to financing to local authorities through (i) adequate and predictable flows of taxes and/or (ii) access to repayable financing.</p> | <ul style="list-style-type: none"> • By the end of 2013, good practices with respect to financial mechanisms for local stakeholders are identified, analysed and disseminated • By 2015, more than half of countries having transferred competence in the water and sanitation sector to the local authorities will have set up a sustainable mechanism allowing local authorities to have direct access for their water investments to i) adequate and predictable flows of taxes and/or (ii) ODA funds. • By 2015, more than half of countries will have set up (or have encouraged or facilitated) a sustainable mechanism for local water operators (private, public, community) to have access to the capital markets for infrastructure investments in the water services. • By 2015, development agencies and financial institutions will have set up | <p>AFD</p> |

| Targets | Target Action Plan Overview | TSG Coordinator |
|--|--|---|
| | specific products and projects addressing the financial needs of local stakeholders. | |
| <p>Target 5: Decentralised financing mechanisms (DSM) By 2015, the resources mobilized through innovative financing mechanisms inspired and promoted by the "1% water and sanitation solidarity levy" have increased by xx%.</p> | <ul style="list-style-type: none"> • By March 2012, a Decentralized Solidarity Mechanisms for water and sanitation Charter is signed; • By March 2012, Global Water Solidarity, the International Platform for the Promotion of Decentralized Solidarity Mechanisms in water and sanitation, is established. • By 2015, DSM is promoted in the water and sanitation international agenda, leading to concrete commitments from key sector actors. | UNDP |
| <p>Target 6: Financing water in an integrated manner By 2015, all OECD countries and 15% of other countries (i) will have financing options for water sustainable cost recovery for agriculture/irrigation water and (ii) will have financing options to ensure the integrity and sustainability of water resources, the environment, and ecosystem services.</p> | <ul style="list-style-type: none"> • By 2015, at least 5 additional countries (compared to 2012) will have initiated private or public private partnership initiatives for more sustainable financing for agricultural/irrigation water; • By 2015, at least 5 additional countries will increase their use of markets and water trading for (i) improved allocation of water resources, and improved sustainable cost recovery for agricultural water and/or water resources management and the environment; • By 2015, at least 20 additional countries will implement systems of environmental taxes and/or tariff schemes that will be earmarked to financing of protection/restoration of water ecosystems. | Agence de l'Eau Artois-Picardie ADB |
| <p>Target 7: Pro-poor innovative financing By 2015, leading services providers, financing agencies and governments in 5 countries : a) are making use of financial and other incentives to provide sustainable water and sanitation services to low income consumers ; b) have mechanisms in place to ensure that capital maintenance and support costs are financed to ensure water and sanitation services that last to low income consumers. This target will be expressed in terms of six key solutions for pro-poor finance of water and sanitation.</p> | <ul style="list-style-type: none"> • By March 2012, leading sector institutions at international and national level sign a "Commitment Charter"; • By 2015, leading service providers in 5 countries sign a formal commitment to apply at least one of the six key solutions in their ongoing management of water and sanitation. | IRC Water and Sanitation for the Urban Poor (WSUP) |



Target 1: Fostering the use of Strategic Financial Planning (SFP)

Target 1 recommends broadening the use of Strategic Financial Planning (SFP) in order to plan the financing of water sector interventions and support the development of reforms. The benefits of SFP arise from the inclusive nature of the process for undertaking a strategic financial plan and the understanding and commitment that is generated amongst stakeholders as a result. The SFP methodology essentially supports a dialogue on improving sector policy and provides an opportunity to build political support for water reforms. The methodology can also be used to foster implementation of policy reforms. It can translate into implementation on the ground when it is linked to decision making, e.g. through budgetary decision-making, donor coordination and dialogue with the private sector (where appropriate).

At present, SFP's use is limited due to limited awareness of its importance and of the existing methodology and tools. The sub-targets proposed by this group therefore focus on increasing awareness and knowledge sharing with respect to SFP. They also aim to obtain commitment from governments and international financial institutions to rely on some kind of SFP process when designing and deciding on the financing of water sector reforms.

The current SFP toolkit is based around a number of tools that require significant amounts of data and a lengthy multi-stakeholder process to prepare the strategic financial plan. Generating data can be one of the major benefits of the process. However, this can also be a daunting and expensive process for countries that do not have institutional capacity. The TSG therefore identifies the need to further develop the toolkit into an "SFP-lite" approach so as to make it useful for such countries. The usefulness of the SFP approach at the local level could be examined, so as to identify if the underlying tools could be refined or modified to address local financing challenges.

The solutions that have been identified as necessary to improve the awareness and understanding of SFP are:

- **Create a knowledge platform on strategic financial planning** that will enable experience-sharing by countries that have undertaken and are considering undertaking SFP;
- **Develop an agreement among major International Financial Institutions and a number of countries that strategic financial planning should be considered as an integral part of the process of providing financial support to the WSS sector** (this can be pursued consistent with the development of "soft measures" identified under Target 2 below); and
- **Further develop the strategic financial planning toolkit** to make it accessible in a cost-effective manner for countries that are resource or data poor, as well as make it useful for local authorities.

Target 2: Ensuring that software costs are adequately financed

There is a strong need for "software" support at all levels of government and other service providers in planning, implementing, monitoring and managing water and sanitation services.

Examples of such "soft measures" include the following:

- **Promoting consensus, creating an enabling environment and clarifying roles of different institutions to enhance coordination and efficiency.** This could include broad sector policy analysis, institutional mapping and expenditure review and medium-term policy and expenditure strategies, focused project action plans, options reviews and business plan development. These soft measures provide stakeholders a way of allocating resources and responsibilities between many different actors.

- **Ensuring sustainability by providing a sound basis for investment and financing decisions.** Where soft measures accompany large investments, these investments are more likely to have been conceptualized and designed appropriately and financial, economic, gender, social and environmental sustainability issues understood and addressed upfront. Clear information around such issues also allows for better dialogue between the public and the private sectors and service users around the best approach to manage risks.
- **Incentivizing accountability and the delivery of good services.** This could include support of regulatory functions, benchmarking and training of water service providers, value-for-money studies and audits, enhancing customer voice and responsiveness of service providers to clients. This type of soft measures plays a key role in enabling the application of global/industry best practice, helping stakeholders' perspectives to be known and addressed and providing an objective basis for decisions on performance.

The level of investment that is required in these soft measures depends on many factors that need to be disaggregated, including specific sub-sector requirements, the local enabling environment, the nature of service provision, whether management is public or private and whether the sector is decentralized.

The target group has identified a number of solutions for the use and financing of soft measures, especially in Zambia, the Philippines and Rwanda. Lessons gleaned about the impact of soft measures in these countries will be presented so as to gain insights on the most effective software measures. A study conducted by the World Bank's Independent Evaluation Group on the development effectiveness of the Bank's analytical and advisory services also provides an interesting solution that will be discussed.

Some of the emerging key messages include:

- The credibility of the soft measure deliverer matters, such as in providing a level of comfort or confidence, international perspectives, and neutrality and objectivity
- Close collaboration with counterparts from task initiation through formulation of conclusions and recommendations is important. The technical quality of a soft measure has a positive influence on the extent to which the soft measure's objectives are met;
- The benefits of successful soft measures usually go beyond those intended, including positive impacts on private investment decisions by domestic and international investors, support for local research, and the creation of informal networks between soft measure deliverers and policy makers.
- Sustained follow-up is one of the most important factors for enhancing the effects of soft measures;
- Useful soft measures can include initiatives that go beyond the WSS sector. For example, a public expenditure review or other studies that examine the impact of WSS on the broader economy could be effective in drawing-in broader constituents and partners.
- Adequate resources are needed to deliver soft measures and to ensure sustained follow-up.

Solutions linked to the dissemination of these key messages include:

- **Identifying and promoting scale up and replication of "essential" soft measures** (e.g. those that foster competition or innovation) as well as other global/industry best practices;
- **Disseminating soft measure lessons to the right audience** (rather than to wider but less-focused audience);

- **Supporting governments’ capacity for effective implementation and sustainability of soft measure** recommendations and ensuring their adequate resourcing;
- **Instituting a mechanism to obtain feedback from governments on a periodic basis**, to encourage a stronger focus on the results of the soft measures delivered;
- Where possible, **linking specific soft measures to a “tangible” output**, such as an investment project, rather than delivered as a stand-alone product.

Target 3: Achieving Sustainable Cost Recovery that is financially sustainable, reliable and socially equitable

Target 3 focuses on the financial sustainability of service providers (be they national or local utilities, municipalities, local independent providers, etc.). It recognizes that the right to water is an empty promise unless these have access to sufficient, reliable and affordable funding to expand, upgrade and maintain infrastructure, access and protect water resources and face exogenous risks (such as climate change or volatile input prices).

The rationale behind Target 3 is that the financial sustainability of service providers depends primarily on the availability of reliable and sufficient revenue from Tariffs, Tax-based subsidies and Transfers from abroad (the OECD's 3 Ts) to cover all relevant and efficient costs, including the financial costs of loans and other repayable finance.

In 2003, the Camdessus report defined “Sustainable Cost Recovery” (SCR) as follows:

- An appropriate mix of tariffs, taxes and transfers (i) to finance capital and recurrent costs, and (ii) leverage other forms of financing;
- Predictability of public subsidies to facilitate investment (planning);
- Tariff policies that are affordable to all, including the poorest while ensuring the financial sustainability of service providers.

Thus, to achieve sustainable cost recovery, providers must still recover all their costs. The new concept introduced by the Camdessus report was simply that this can be achieved through a combination of three revenue streams and not only from tariffs. It is important to note, however, that the 3 Ts are not perfect substitutes and that tariff revenues remain important for a number of reasons. First, financial sustainability is directly related to the financial independence of providers, which can be weakened by their dependence on subsidies and grants, unless the reliability of these two sources of revenue is ensured. Secondly, the 3 Ts provide very different incentives to water users. Only tariffs can send a signal to users that water is a scarce resource that needs to be efficiently used, while wastewater charges are consistent with the polluter-pays principle. Finally, tariffs provide a direct link between providers and their customers and should therefore help increase responsiveness and accountability towards them.

Target 3 calls for the implementation of SCR strategies, which are made up of:

- A clear methodology to compute relevant and efficient costs;
- A complete tariff strategy, that identifies and balances competing policy objectives;
- Reliable, predictable allocations from national or local budgets;
- Access to predictable, targeted grants from abroad (where available).
- In turn, a complete tariff strategy is composed of three elements:
- Average tariff levels, whose main goal is to contribute to financial sustainability;

- A tariff structure that can be designed to address social, economic and environmental concerns. To achieve social concerns linked with affordability of services for the poor, it is preferable to couple targeted tariff-based support with non-tariff mechanisms;
- A process and methodology for tariff-setting and adjustment, including appropriate communication and public consultation.

The solutions that will be discussed at the Forum can be classified according to the actions that are needed to implement a successful SCR strategy, including:

- Clarify: (i) A **Glossary on SCR and financial sustainability**, as a common language is needed to reduce polarised discussions on this issues, (ii) **A toolkit on “SCR for practitioners”** to clarify multiple objectives and the roles / responsibilities for each stakeholder (national and local authorities, regulators, utilities, consumers/civil society, financiers..), (iii) Their **dissemination by a multi-stakeholder coalition**, preferably in coordination with the platform for SFP promoted under Target 1;
- Quantify: (i) a **clear methodology to compute all relevant and efficient costs of service provision** (including resource and uncertainty costs), (ii) comparison of **indicators of financial sustainability of service providers in view of introducing a “SCR label”** and its associated tracking system, (iii) examples of tariff-setting formulas;
- Scale-up: **examples of successful SCR strategies from different regions that have the potential for being scaled-up**, including actions by utilities (Cambodia, Portugal), governments aiming at increasing reliability of transfers (Ethiopia, Ghana) and new instruments to meet the challenges of separate wastewater services (Tunisia);
- Support: **examples of the use of tariff structures and income-support mechanisms** aimed at ensuring affordability of services for the poor (Zambia, Flanders);
- Regulate and communicate: **identify regulatory systems and public consultation processes** from which lessons can be learned (Portugal and examples from Latin America).

Target 4: Providing access to financing to local stakeholders

Recognising the fact that the provision of water and sanitation services tends to be increasingly decentralised, Target 4 focuses on the need to ensure that local authorities have access to sustainable flows of funding to meet their obligations to ensure efficient service delivery.⁶

The TSG has reviewed more than 30 interesting experiences of financing mechanisms for local stakeholders originating from more than 20 countries in Africa, Asia and Latin America. This includes, on the one hand, existing experiences that have already proven their effectiveness and added value, and, on the other, innovative experiences that are still at the experimental stage.

⁶ The session for Target 4 has been combined with “Priority for Action # 1.4., Target 4”, which states: “By 2015 more than half of countries in each continent have set up financial mechanisms that suit the needs of local authorities and local operators”. As a result, the session will examine financing mechanisms for all types of local stakeholders, including municipalities, municipal or decentralized public water (and sewerage) utilities, local small and medium enterprises and water users committees.

Some of these existing and innovative experiences that have been tested in different countries have been classified in three main types of solutions:

- **Mechanisms to establish predictable flows of subsidies.** The central question here is how to assist local governments that do not have the resources to be self-financing or have an adequate tax base. In this regard, central government can help establish a positive more environment for municipal financing by better defining the system of intergovernmental transfers and shared taxes and making it more predictable. This also includes mechanisms to channel taxes and transfers to local stakeholders. These include national water trust funds and long-term partnerships between water utilities or municipalities in developing countries and their peers in developed countries.
- **Basket funds mechanisms to address the small and medium towns (SMTs) needs.** These include mainly access to the domestic capital markets through sub-sovereign loans from IFIs and revolving fund mechanisms. The case study of the revolving fund in Ethiopia will be particularly developed.
- **Mechanisms that enhance an appropriate banking market and enhance the bankability of local entities through pooled bond issuance.** These include an appropriate banking supply, providing credit in the form requested by the WSS sector, i.e. with long term loans at low interest rates. Indeed, whereas many countries have made access to credit by local entities a hallmark of their decentralization policy, most countries that allow local borrowing have established debt limits intended to keep local authorities from borrowing irresponsibly. Many prohibit local authorities from borrowing in foreign currencies. Examples of solutions examined as part of this target include the **Indian experience to support municipal bond issuance**, or **instruments**, established with USAID and JICA, **to help fill service gaps by leveraging financing in the Philippines**.

Target 5: Supporting the development of Decentralised Solidarity Mechanisms

Target 5 recommends the development of decentralised solidarity mechanisms based on the “1% water and sanitation solidarity levy” introduced in France via the Oudin-Santini law adopted in 2005. This initiative has already been replicated in a number of Western European countries, such as Switzerland ([Plateforme Solidarit’eau](#), an internet platform established in September 2007), the Netherlands (law “Motie Koppejan” in 2008), Spain (“canon del agua”), Italy and Belgium.

Decentralised Solidarity Mechanisms (DSM) aim to fill at least part of the existing technical and financial gap for water and sanitation services at the local level. On a voluntary basis, local governments (typically located in the North) agree to facilitate access to financial resources, capacity building and technology transfers as a gesture of solidarity and support to sub-national institutions and local governments (typically located in the South).

The Target focuses on the establishment of an institutional basis for a progressive expansion of DSM in the field of water and sanitation. To reach this objective the TSC focus its efforts on two lines of actions:

- **The establishment of the International Platform for the Promotion of Decentralized Solidarity Mechanisms in water and sanitation (IPPDMS).** The specific objective of the IPPDMS is the development, diffusion, replication and scaling up of existing water and sanitation DSM;
- **The promotion of DSM in the water and sanitation international agenda, leading to concrete commitments from key sector actors**, including local authorities, national governments, specialized public agencies, private institutions and civil society organizations from the water and sanitation sector. These commitments will facilitate the

creation of an enabling environment for the development of decentralized solidarity mechanisms.

The International Platform will be based on the following instruments:

- Creation and promotion of a **certification and registration system** for DSMs based on principles predefined by the Platform. These principles are likely to include: universality, subsidiarity, additionality, leverage, institutional, environmental and financial sustainability. A certification a “label” will be developed and granted to concrete international initiative on the basis of adherence to these pre-defined principles
- An **international Charter** in line with the objectives and principles promoted by the Platform, to facilitate the mobilisation of political institutions that have competencies in the water and sanitation sector and for the promotion of DSMs. This will be presented at the 6th World Water Forum;
- **Knowledge management tools facilitating technical cooperation and exchanges of good practices and lessons learned in the development of DSM.** This includes the possibility of creating an international community of practice on water and sanitation DSM and/or a database with case studies of innovating initiatives at local (subnational authorities engaged in DSM, etc.), national and international level.
- **An on-demand technical network for the identification and facilitation of technical cooperation opportunities** among several actors committed or interested in the development and extension of the DSM.
- The **participation in major international fora and regional processes**, among others the 6th World Water Forum in Marseille, Rio+20 and the WACAP Forum, in order to promote the debate on the role and contribution of DSM to improve access to water and sanitation services.

The role of the international Platform will be to facilitate the communication among existing and/or developing national platforms in the field of water and sanitation. It will aim to reinforce the scope, actions and visibility of existing national platforms. In countries without existing DSMs, the Platform can stimulate and accompany their creation by providing direct technical support to local, regional, national, continental institutions or facilitating technical exchanges with other existing platforms.

A second result will be directly linked to the promotion of decentralized solidarity mechanisms in the water and sanitation international agenda and the achievement of concrete commitments from local authorities, national governments, specialized public agencies, private institutions and civil society organizations from the water and sanitation sector. These commitments will facilitate the creation of an enabling environment for the development of decentralized solidarity mechanisms.

Target 6: Financing Water in an Integrated Manner

Target 6 examines the specific challenges raised by the financing of water in an integrated manner and for ensuring the integrity and sustainability of water resources, the environment and ecosystem services. This target examines water needs for all the sectors, including for agriculture, domestic use, industry, energy production, recreation and the environment. All water uses are dependent upon the effective overall management of the resource. A particular focus is the financing water for agricultural and irrigation purposes. Target 6 has identified a number of innovative solutions to tackle those challenges, as summarised below.

Environmental taxes to support payment of ecosystem services are based on water abstraction and/or polluted water discharged and is a solution that can be widely adopted for financing water resource management. The level of the taxes is calculated based on the level of abstraction and the quantity/type of polluting parameters. The money raised through these taxes can be earmarked to finance measures to reduce pollution (e.g. treatment of waste water) in the ecosystem and to restore ecosystem (e.g. soft management of rivers) that provides services. French Water agencies have implemented these taxes for more than 45 years based on the polluter-pays principle and the French Water law adopted in 1964. At River Basin Level, the six French Water Agencies are collecting taxes (“redevances”), under the control of River Basin Committee. These taxes are earmarked for mitigation and restoration measures for ecosystems. This solution provides an effective and economically efficient way to provide financing for the protection and restoration of the environment and ecosystems services. This solution also includes a strong pricing signal linked directly to the use of water and pollution of water within the river basin. The OECD and other agencies have strongly supported this approach based on the polluters pay principle through numerous publications.

Payment for eco-compensation between upstream water providers and downstream water is also a solution for integrated financing to help ensure the integrity of the watershed and support water resources management. Eco-compensation not only shares characteristics with payments for ecological services, but also encompasses fiscal transfer schemes between provincial governments to improve the apportioning of funding and clarify responsibilities and tasks on environmental management. In particular, this can be applied to ecological service flows that cross administrative and regional boundaries, such as watershed ecological services. Such innovations have been at the core of the Chinese government’s ongoing efforts to identify and address the institutional drivers of the People’s Republic of China’s water crisis. The eco-compensation scheme for integrated river basin management is expected to be implemented nationwide, involving the central government and multiple provincial agencies. The PRC’s central government has tasked the National Development and Reform Commission (NDRC) to develop the national Eco-Compensation Ordinance. The Asian Development Bank has committed to supporting these efforts through the provision of technical assistance to the PRC to help support the legal framework and develop further the institutional framework. It is anticipated that this solution can be replicated in other ADB member countries based on the experience and lessons for the PRC.

Treating irrigation systems as integrated water service systems with multiple customers who derive different benefits and returns from water use is a solution that can increase sustainable cost recovery and lead to improved water resources management. A recent FAO (2010) study of 34 large irrigation systems found that only two such systems were single use while the others supported livestock, domestic water supply, large and small industry, hydropower, transportation and ecosystem services. The benefits per unit volume of water used varied significantly for each user, however. Introducing different pricing options to improve financial returns from higher value uses can improve operating cost recovery and investment. For example, the “financing for multiple water services approach” based on MASSMUS (Mapping Systems and Services for Canal Operation Techniques) has fostered improved water resources management and a more service-oriented approach for the system operator, who needs to balance competing uses and ensure financial flows. Enabling this approach requires an in-depth analysis of the system’s water balance and various uses. An example of this can be seen in the Fenhe irrigation district in Shanxi, China. FAO has committed to finalizing and publishing the methodology and supporting documentation in 2012 and will promote the scheme with its clients and in cooperation with its development partners. It is anticipated that this solution can be widely adopted in large irrigation schemes through commitments from irrigation managers, local Governments, and decision makers at the national and provincial levels.

Although it has not yet had widespread use, **public private partnership (PPP) also provide an important solution for improved irrigation financing** as the demand for food and irrigated agriculture continues to increase. Like for water supply and sanitation services, the enabling framework to support PPPs first needs to be in place for this approach to be successful. The world's first purely PPP irrigation project is the 10,000 hectare Guerdane Irrigation system in Morocco finalized in 2004, which provides a good model for scaling up. In its Operational Plan for the Water Sector 2011 – 2020, the ADB has committed to increasing private sector participation to a larger part of its operations to help address the estimated 40% financing gap for water investment in Asia by 2030. This not only includes water supply and sanitation but a concerted effort to find innovative ways to engage the private sector for agriculture/irrigation water and water resources management. The ADB's Asia Irrigation Forum scheduled for April 2012 will explicitly address PPPs and third party arrangements as options for strengthening irrigation service delivery. In future, it is anticipated that as the private sector and governments gain experience, they will start to innovate and develop projects without external assistance.

The use of water resource markets is an emerging solution for the allocation and pricing of water resources in developed economies throughout the world. Australia has been developing its market system for over 20 years, and it has been successful on many fronts, including financing. The preconditions and enabling environment to support effective and efficient markets are integral to the solution. Commitment from all stakeholders is required to trial different approaches and to pursue incremental improvement over time. TSG 6 discusses water markets in Australia and the opportunity for scaling up the use of markets to support integrated financing for agriculture, water resource management and the environment. To support this work, the ADB will be developing a framework to (i) assess the current status of the enabling conditions as well as (ii) the required reforms and institutional and capacity development to help promote the development of market mechanisms for water management. It is recognized that market mechanisms may take a long time to be adopted effectively and they are likely to be more relevant for more developed countries. However, as many middle income countries are developing rapidly, raising awareness and putting the enabling framework in place is the first step to implement the solution.

The ADB Water Operational Plan 2011-2020 is setting out a few actions and principles that will foster adoption of these solutions to achieve the targets. The Plan also calls for enhanced analytical work to support this, including a “Future of Water in Asia” report that looks at key trends across Asia in all sectors, including agriculture and irrigation and the environment and ecosystem services. This will provide a platform for dialogue to discuss the issues directly related to the solutions above and provide guidance on how countries can commit to these solutions.

The second piece of analytical work will consist of detailed country water assessments for key ADB member countries, in order to develop more detailed strategies and actions. Both the draft of the “Future of Water in Asia” report and the first set of country water assessments should be drafted by 2015. It is anticipated that this awareness raising and policy dialogue will also lead to ADB technical assistance and investments to implement the solutions. ADB will host the Asian Irrigation Forum in April 2012 for its clients and other stakeholders that will promote the irrigation/agriculture solutions for TG6. ADB will track the progress of the solutions through its ongoing operations and reporting for the Water Operational Plan 2011 – 2020. The TSG is also open to commitments by other stakeholders and will dialogue with them to forward the solutions that will help achieve the targets.

Target 7: Reaching the poor via innovative financing mechanisms

Target 7 identifies innovative financing mechanisms that can help provide water and sanitation services for “hard-to-reach” low-income consumers, in rural, peri-urban and urban areas. Based on an extensive review of potential solutions, the TSG has identified six solutions that they deem to be especially useful to achieve those objectives, which are backed up with case studies in which these solutions have been successfully applied in practice. A key argument of the TSG is that pro-poor financing approaches must necessarily be financing approaches that guarantee post-construction financial sustainability. To give a simple example, one-off subsidy financing of water pump construction is of no real value if there is no mechanism in place to generate funds for ongoing pump maintenance and eventual pump replacement.⁷ The six “key solutions” outlined by the TSG are briefly summarised below.

Achieving sustainable pro-poor finance through Life-Cycle Cost Analysis. At present, very limited knowledge exists on how much poor households pay each month for operation and maintenance services, and whether these amounts are adequate to meet costs of operation and maintenance, and at the same time affordable to users. The TSG suggests that detailed assessment of life-cycle costs is critical as a basis for pro-poor finance solutions and identifies cases where this has been done successfully, such as in South Africa or Brazil. This can start by looking at unit costs to serve the poorest of the poor within a given district or community, and to assess the differences between ‘designed-for’ and ‘received’ quality of service.

Achieving sustainable pro-poor finance through maximisation of local small-scale private-sector involvement. There is broad consensus that local small-scale private-sector entrepreneurs can make very important contributions to sustainable pro-poor services, particularly in urban communities. Yet, channelling financing to these small-scale actors can be particularly challenging. The TSG presents a number of solutions to address this issue, a) through support of small-scale delegated management models (citing the example of the Naivasha delegated management model, a project designed with WSUP support in Kenya), b) through sanitation marketing initiatives (citing an IDE supported project in Vietnam), and c) through microfinance programmes that offer lines of credit to the local community operators of water and sanitation services (as in the Community Development Fund in Ethiopia).

Achieving sustainable pro-poor finance through innovative tariff systems. In many cities in sub-Saharan Africa and Asia, water tariff systems often simultaneously fail to achieve both financial sustainability and pro-poorness: a common situation is for per-litre tariffs to be too low to achieve genuine financial sustainability, while connection charges are too high for poor consumers. The most common solution is technically simple, though it may be politically difficult: ensure that per-litre tariffs are high enough to achieve city-wide financial sustainability, and reduce connection fees for low-income consumers, as done in Mozambique where national institutions are strongly committed to rationalising tariff structures. Other innovative tariff structures can be implemented such as in Flanders (Belgium), with first, a fixed allocation of a certain volume of water at no charge to the consumer, and second, the granting of exemptions from sanitation charges for low-income households.

Achieving sustainable pro-poor finance through cross-subsidy and bundling. In many developing countries, sewerage coverage is very low and households need to cover the costs of their on-

⁷ This is in line with the emphasis on Sustainable Cost Recovery (SCR) emphasis that underlies Target 3.

site sanitation systems. This basically eliminates the potential for cross-subsidies between water and sanitation that is commonly practiced in systems where these two services are combined. The proposed solution consists of cross-subsidising the costs of onsite sanitation from water revenues, such as practiced in Ougadougou (Burkina Faso), Dakar (Senegal) and Manila (the Philippines). In Manila, for example, water consumers connected to sewerage pay a 50% surcharge on their water bill and all water consumers pay a 10% "environmental surcharge", which is used for provision of desludging services in all parts of the city, including low-income neighbourhoods.

Achieving sustainable pro-poor finance through Output-Based Aid (OBA). An increasingly well-known solution for pro-poor concessional finance is Output-Based Aid (OBA). Under a typical OBA agreement between a financing institution (e.g. a development bank) and an implementing agency (e.g. a water-sector asset holder), disbursement of funds for infrastructure construction is withheld until verification of infrastructure construction and operations. OBA has been used for water but comparatively less so for sanitation. The TSG refers to an example where OBA has been used to support water and sewerage services provision to low-income communities in three Moroccan cities. Other types of results-based financing mechanisms may also be appropriate and to be developed. The TSG notes a few limitations of the OBA approach. On the one hand, the operator needs to pre-finance the service (and some weaker operators may not feel confident to do so. On the other hand, the OBA approach is very focused on supporting initial construction and insufficiently on operational sustainability.

Achieving sustainable pro-poor finance through Progress-Linked Finance. Based on the observation that OBA may not be applicable everywhere, the TSG proposes an alternative approach, referred to as Progress-Linked Finance (PLF). In very simple terms, PLF can be summarised as an agreement of the following type: "If the service provider can demonstrate 3 years from now that they have met conditions A, B and C in relation to financial viability and pro-poor commitment and capacity, the financing institution will provide a grant or loan of amount X for WASH scale-up". Central to the model is positive incentives coupled with rigorous verification that conditions have been met. The lack of major pre-financing requirement makes it accessible even to service providers that do not currently have access to substantial concessional funding. The PLF approach has been recently developed by WSUP and has not yet been tested at scale. However, broadly similar approaches are often applied in development bank programmes (where they may be termed "milestone agreements" or similar), or may be integrated into intra-national water and sanitation programmes. In the Philippines, for example, the 'Graduation' concept has been developed to incentive operational and financial improvement among Water Service Providers.

The TSG will seek broad commitment to these six key solutions from institutions throughout the sector. More concretely, specific formal commitments will be sought from service providers in 5 countries selected from among IRC and WSUP's African focus countries to implement these types of solutions. All institutions and service providers involved in these commitments will be organisations with which IRC and WSUP will be maintaining close relations over the coming 4-year period, such that it will be feasible to integrate follow-up and monitoring of progress towards these commitments into their work programmes at minimal cost. Thus, the TSG coordinators IRC and WSUP will directly manage and support specific commitments. However, this should be considered an open process, and the TSG is entirely open to parallel commitment to the six key solutions by other organisations and for follow-up after the Forum towards the 2015 proposed targets.


Overview summary of solutions

In summary, the solutions proposed by the TSGs broadly fall into three main categories:

- **Clarify and disseminate:** solutions that consist of clarifying and disseminating commonly accepted principles and approaches, with specific tools to facilitate their adoption and sharing of experiences with implementation;
- **Scale-up:** solutions that consist of scaling-up successful approaches that have so far been adopted in only a limited number of countries;
- **Innovate and pilot-test:** solutions that have yet to be tested but nevertheless appear to be promising.

Table 2 below presents examples of solutions that fall into each of these three categories.

> Table 2 – Overview summary of solutions proposed through CS2

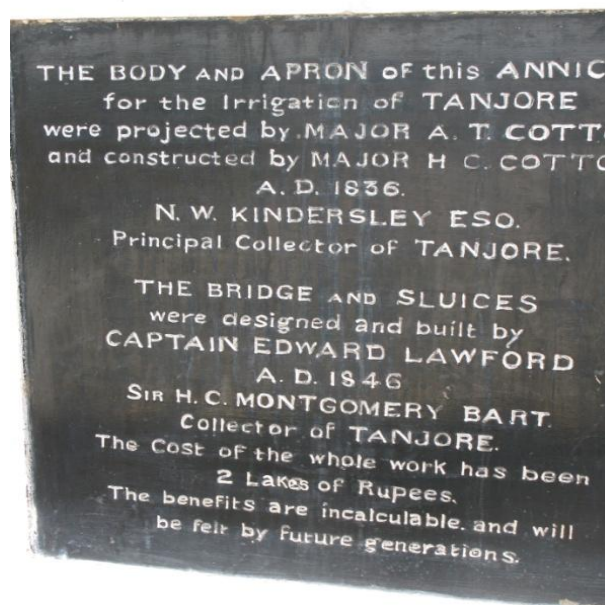


| Targets | Clarify and disseminate | Scale-up | Innovate and pilot |
|--|---|---|--|
| Target 1 – Strategic Financial Planning (SFP) | <ul style="list-style-type: none"> SFP toolkit Knowledge platform on SFP for experience sharing | <ul style="list-style-type: none"> Commitment by governments and international organisations to include SFP into planning | |
| Target 2- Financing Soft Measures | <ul style="list-style-type: none"> Identify common characteristics and examples of “essential” soft measures Disseminate findings and lessons of soft measures to the right audience(s) | <ul style="list-style-type: none"> Scale-up “essential” soft measures as well as other global/ industry best practices Support governments’ capacity for the effective implementation and sustainability of soft measure recommendations | <ul style="list-style-type: none"> A mechanism to obtain feedback from governments on a periodic basis to evaluate the benefits of soft measures |
| Target 3- Sustainable Cost Recovery (SCR) | <ul style="list-style-type: none"> Glossary on financial terms Toolkit on SCR for practitioners Check-list on SCR for decision-makers Manual with indicators of financial sustainability of service providers (for utilities, regulators, local authorities...) | <ul style="list-style-type: none"> Experiences of financially sustainable utilities (Pnom Pehn, EPAL) Tariff structure reforms associated with non-tariff mechanisms (Flanders) Role of national and local regulators to de-politicise tariff adjustments (Portugal, Latin America) Communication and participatory strategies, role of different parties (Portugal) New mechanisms for reliability of tax-based subsidies (Ghana SWAp, Ethiopia local bond) | <ul style="list-style-type: none"> SCR label for sustainable service providers and tracking system Financial Institutions agree to focus on process-based milestones based on common definition of financial sustainability (plus soft support for policy dialogue on SCR) Non-conventional sources of revenues for providers of wastewater services (payment for ecosystem services, sale of treated WW for reuse/recharge of aquifer) |
| Target 4 – Local-level Financing | <ul style="list-style-type: none"> Prepare guidelines for improved mechanisms, and present / discuss them in regional seminars in every continent | <ul style="list-style-type: none"> Mechanisms channelling predictable subsidies to local authorities, as implemented in Colombia Basket fund mechanisms such as the one implemented in Tanzania or Ethiopia Mechanisms enhancing an appropriate banking supply and the bankability of local entities, for example through pooled bond issuance as in the India (Tamil Nadu) case | <ul style="list-style-type: none"> Guidelines for financial support to local stakeholders |

| Targets | Clarify and disseminate | Scale-up | Innovate and pilot |
|---|--|--|---|
| Target 5- Decentralised Financing Mechanisms | <ul style="list-style-type: none"> • International Platform for the Promotion of Decentralised Solidarity Mechanisms • International charter, knowledge management tools | <ul style="list-style-type: none"> • Promotion of DSMs in national agendas | <ul style="list-style-type: none"> • Certification and registration system for DSM • On-demand technical networks |
| Target 6 – Financing Water in an Integrated Manner | <ul style="list-style-type: none"> • FAO methodology for financing from multiple irrigation systems • Financing for IWRM in the Lao PDR | <ul style="list-style-type: none"> • FAO methodology for financing from multiple irrigation systems • Payment for ecosystem services in the PRC • French taxes and tariffs for ecosystem services | <ul style="list-style-type: none"> • PPP for irrigation in Morocco • Market mechanisms from Australia |
| Target 7 – Pro-poor Innovative Financing | | <ul style="list-style-type: none"> • Analyse life-cycle costs (Brazil) • Cross-subsidise on-site sanitation from water (Ouagadougou, Manila) • Output-based aid for sanitation (Morocco) | <ul style="list-style-type: none"> • Progress-Linked Finance |

3.2. Examples of promising solutions in need of further commitments

Implementing the proposed solutions will require a firm commitment at political level to increase overall levels of funding to the sector. In the context of the economic and financial crisis, this will be even more demanding than at the time of the Camdessus report. Mobilising the political will of governments (in the North as in the South) will require making the case for allocating financial resources to the sector, a long-term investment that can create jobs in the short term (for construction as well as operations and maintenance of infrastructure and provision of associated software services) and generate benefits over many generations. This was very apparent to the builders of dams and sluices in the State of Tamil Nadu in India, who dedicated a plaque to those who had been involved in its construction (to the right).



Legend to the picture: A plaque dedicated to Major Cotton, the designer of a bridge and sluices in Tamil Nadu (India) at the time of the British Empire outlining that, even though the costs might have been substantial, “the benefits are incalculable and will be felt by future generations”. Politicians always need to be reminded of this basic fact.

National governments looking to convince their Ministries of Finance to allocate funding to the sector or donor governments will have to justify their aid budgets and sectoral allocation also need to develop value-for-money arguments, particularly in times of economic hardship and spiralling public debt, in order to protect funding to the water sector. This can be assisted by value-for-money estimates, estimating the costs and benefits of specific investments. To complement these economic estimates, Government will also need to estimate the actual monetary benefits that these investments confer beyond the potential economic benefits.

One critical issue at this stage, however, is that there is no commonly accepted methodology for tracking financial flows to the water sector, which makes all of these calculations very difficult to carry out. For example, in 2008, Sub-Saharan African countries committed to spending 0.5% of their GDP on sanitation via the eThekweni declaration. As there is no commonly accepted methodology for compiling this figure, however, the ability to monitor delivery against such an important commitment is very limited. The sector is much behind in this area, compared to other sectors that are competing for resources such as health or education. WHO, through the 2012 GLAAS report is proposing to form a “coalition of interested organisations” that could jointly develop a commonly accepted methodology for tracking financial flows, as it has been done successfully in the health sector. They propose a methodology for doing so and suggest that this methodology be launched and scaled up in the coming years, a very worthwhile exercise that would require support from a broad range of organisations in the sector, to help with the development of the methodology and identifying practical cases for its application.

4. Outline the limits of the approach and areas to be further investigated

The proposed targets and solutions could not seek to address all areas through which sector financing could be improved. The proposed solutions are mainly focused on mobilising financing through the 3Ts and defining a sustainable mix of all potential financial resources in order to achieve sustainable cost recovery. These solutions all converge to the over-arching aim of increasing financial resources to the sector, including from tariffs, taxes and transfers based on international aid or solidarity funds. Such an increase will require political will and determination. For example, the High Level Panel on Finance organised at the World Water Forum will examine in particular the much needed increase in transfers to the water and sanitation sector, to identify new sources of funding.

A number of more specific areas could not be dealt with in much detail within the scope of this exercise, as they may be addressed elsewhere or because they fell outside the scope of our investigation. Below, we identify a few areas that would merit further investigation in future or in other instances:

- **Addressing** Addressing the specific financing needs of some key “sub-sectors”, such as the sanitation and hygiene sector or the investments required to adapt to climate change;
- Mobilising repayable financing via innovative financing.

The specific financing needs of some key “sub-sectors”

Until fairly recently, the debate on financing “water” was more often than not a debate about financing investments in developing water supply services. The works of this group have sought to depart from a narrow view of “water financing”, by considering financing needs for other sub-sectors (for example, agricultural water), of the environment itself or financing soft measures.

However, what is apparent is that the “water sector” is a very diverse and complex sector, and each of its “sub-sectors” call for specific financial arrangements depending on the fundamentals of service provision. For example, the issue of “financing sanitation” has risen to the fore since the International Year of Sanitation in 2008 and other international initiatives which greatly contributed to placing the spotlight onto sanitation needs in general and fostering the development of new and innovative approaches to sanitation service provision in particular. Financing sanitation raises specific challenges because demand for sanitation is more difficult to generate and it is impossible to disconnect a sewerages service in case of non-payment.

In addition, in most developing countries, on-site sanitation systems are much more prevalent than network (or off-site) systems and are likely to remain so for the near future. The sanitation financing equation has therefore much more to do with giving incentives to households to invest in their own sanitation solutions (sometimes combined with facilitated access to finance) rather than for the public sector to invest itself. The latter would therefore require more soft measures than hardware investments, a change of mindset that is often difficult to bring about at the level of development countries’ central and local governments. An emphasis on soft measures would also be required for financing hygiene activities, which are themselves critical given the evidence that handwashing with soap can be hugely beneficial, even perhaps more so than drinking clean water or keeping to fixed-point defecation points.

Other sub-sectors for which a specific financing approach may need to be developed including financing for the agricultural sector and environment through the use of market mechanisms for allocation or financing climate change adaptation (via identifying new financial sources).

Mobilising repayable financing via innovative financing

On the whole, the group did not deal in detail with innovative financing mechanisms that can be used in order to mobilise repayable financing, such as commercial bank finance (for example, through the use of guarantees) or microfinance. For example, Target 7 refers to microfinance institutions as potential channels for government subsidies (as in the case of the Community Development Fund in Ethiopia) rather than as providers of new sources of finance.

The Camdessus report released in 2003 included a long list of recommendations on how new financial sources could be attracted to the sector, how they could be channelled to different types of recipients (and in particular, local governments) and how the environmental policy environment could be improved to make the sector more attractive to repayable finance.

While significant progress has been made on implementing a number of these recommendations (such as the development of sub-sovereign lending), more efforts and time for implementation are still needed. Almost ten years down the line, few of the recommendations contained in the Camdessus report have been adopted in a comprehensive way or led to radical changes in financing policies and practices. At the operational level, worthwhile initiatives have been taken in order, for example, to increase the use of guarantees or spread the use of revolving funds. These initiatives have remained at a limited scale, however, and have not been sufficient to attract new sources of financing in a significant way.

The sector is comparatively little known by commercial finance providers and there is often a discrepancy between long-term investments needed in the water sector to match the life of the assets and the short-term lending capabilities on local markets. Informal operators, who serve an average of 50% of the population in developing countries according to Kariuki & Schwartz (2005) have difficulties in accessing credit from the conventional banking sector. In addition, as highlighted in OECD (2009), the water sector combines a number of substantial risks, such as commercial risk (related to revenue), contractual risk, and foreign exchange risk that make equity capital and debt financing from international markets expensive and deter commercial funding. Innovative financing can play a major role to attract market-based repayable finance to the sector. Below, we mention some examples of such innovative financing mechanisms.

For example, microfinance could be a key way to overcome affordability constraints for providing access to services, particularly for households and small-scale water providers in developing countries. The use of microfinance has so far been limited in the water and sanitation sector, partly due to a lack of awareness and limited understanding on the part of microfinance and water sector professionals of their respective sectors. A review by Mehta (2008) made the case for the strong potential of microfinance in the sector, particularly for loans to households and to community projects (such as slum redevelopment projects). The provision of foreign transfers (ODA) could play a role in developing the use of microfinance for WSS by providing seed financing to revolving funds or microfinance institutions, smart subsidies for product development or guarantees. Donors and IFIs could help build awareness of microfinance products, through capacity building activities or blending microfinance with other types of financing instruments in the projects they choose to support. For example, they could combine reliance on microfinance (or local commercial banking in the case of small-scale entrepreneurs) with Output-Based Aid, i.e. subsidies paid based on effective and measurable results to service providers, which would therefore be more incentivised to deliver results.

Another area that still needs to be explored is how to increase the use of guarantees. Although a whole array of guarantees and insurance products are available from donors, IFIs and private

institutions, they have not been used on a regular basis or at a large scale in the water sector. This partly reflects the changing structure of the market for water services: whilst international private operators have largely withdrawn (except from a few booming markets, particularly in South-East Asia), guarantees provided by international institutions for relatively large “transactions” are less appropriate than they might have been during the “heyday” of international private sector participation in the water sector. Besides, IFIs and donors have usually maintained fairly rigid rules about the use of these guarantees (for example, with counter-guarantee requirements or restrictions on the provision of stand-alone guarantees), which means that transaction costs for applicants remain high. The establishment of “guarantee facilities” at national level, to which donors and IFIs contribute seed financing or overall guarantees (as done with LGUGC in the Philippines) could facilitate the provision of guarantees at the local level, which is more in line with the current market structure in the water sector. Donors and IFIs may also need to step in where private entities or governments have become less willing to provide guarantees.

Raising equity could also help strengthen the balance sheets of water companies, which are often under-capitalised. Interesting models have been developed in the water sector to mobilise equity via financial markets (such as the Hyflux Water Trust in Singapore), thereby diversifying away from mobilising funds from private water companies (whose ability to bring in equity capital is limited in any case) and using such equity injections to leverage other forms of finance for capital investments. Mobilising equity through capital markets can strengthen financial discipline and improve transparency, including for companies that are primarily government-owned (including a number of State Water Companies in Brazil, which are publicly listed). When requested to provide equity in distressed situation, many donors tend to be reluctant to do so as such equity contributions can sometimes be treated as an implicit subsidy when return expectations are very low. However, as long as financial discipline is maintained, equity contributions can strengthen the balance sheet and provide a sound basis for leveraging additional forms of finance, such as loans and bonds. In such selected cases, IFIs and donors can make such equity injections themselves, including in some cases by swapping debt for equity.

In the current context of a persistent and global economic crisis, mobilising such financing may appear even more difficult than when the Camdessus report was written. However, the overall context following the crisis could potentially be conducive for more market-based finance to be allocated to the sector. On the one hand, private capital’s appetite for risk has gone down and preferences have shifted away from high risk/high returns investments to those with lower but steady and guaranteed cash flows, which is a distinctive feature of well-managed water companies. In addition, given the renewed emphasis on protecting natural resources, the long-term strategic value of preserving and improving access to water is increasingly recognised.

Finally, the boundaries between the public and private sectors have been blurred and the controversial nature of the debate on PSP has abated somewhat, with more dialogue going on at sector level and the recognition that a number of reforms are required regardless of ownership. In that context, market-based finance can potentially make a significant contribution to bridging the financing gap in the water sector, for private and public water service providers.

5. Recommendations for follow-up post 2012

This section puts forward recommendations to ensure a productive follow-up and monitoring of the commitments and implementation of targets and solutions between 2012 and 2015.

The working group that has supported the development of the targets is not proposing to continue to function in its current form. Instead, the platforms that will be formed for each target will be taking the work agenda further. Reporting back on activities undertaken under CS2 could be done at the 2015 World Water Forum in South Korea.

Instead, each of the target groups will put in place some specific monitoring arrangements depending on the type of commitments that has been entered into. Table 3 below summarizes those commitments and monitoring arrangements put in place by each target group. Some of the commitments are limited to the organisations that have been leading work on the particular target, others are broader and could be considered as pledges. Many of the groups are looking to the stakeholders meetings in Marseille in March 2012 in order to help better define the pledges, commitments and monitoring arrangements.

> Table 3- Overview of commitments and monitoring arrangements



| Targets | Commitments | Monitoring arrangements |
|---|--|--|
| Target 1 – Strategic Financial Planning (SFP) | Develop a web platform for pooling of country experiences on strategic financial planning. Obtain an agreement amongst International Financial Institutions and countries on need for strategic financial planning as an integral part of water sector planning and financial support. Investigate the extension of the strategic financial planning toolbox to address data and cost concerns. | To be developed with relevant stakeholders at Marseille and beyond. |
| Target 2- Financing Soft Measures | Identify solutions for estimating how much and how soft measures are being funded in a way that maximizes the chance of continuity into the future or until needed. Support soft measures that respond to a relevant and wide-spread issue in the sector and demonstrate effectiveness in doing so. Arrive at specific soft measure solutions that can be worked at scale – e.g., fostering competition or innovation. | To be developed with relevant stakeholders at Marseille and beyond. |
| Target 3- Sustainable Cost Recovery (SCR) | Glossary and toolkit/checklist disseminated in conjunction with SFP platform SCR label for sustainable service providers established together with tracking system Financial Institutions agree to focus on process-based milestones based on common definition of financial sustainability (plus soft support for policy dialogue on SCR) | Tracking system for label to be discussed with IWA in Marseille if idea is confirmed Special reports on support for and effectiveness of process-based conditionalities |
| Target 4 – Local-level Financing | Large dissemination of good experiences and practices in order to achieve the target | Good practices and guidelines for improved mechanisms are presented, discussed and disseminated at regional seminars |
| Target 5- Decentralised Financing Mechanisms | Partners sign International Charter for the promotion of DSM Support a further development of existing DSMs and, overall, facilitate the necessary elements to trigger and facilitate the creation of new DSMs in other countries and regions with a special focus on Asia-Pacific and Africa | Global Water Solidarity platform leads activities, coordinates and follows-up to facilitate the implementation of engagements, including those in the Charter |
| Target 6 – Financing Water in an | “Future of Water in Asia Study” and ADB country water assessments published Enhanced private sector engagement and financing for irrigation and/or environment and ecosystem services | ADB reporting for its Water Operational Plan 2011 – 2012 and other internal and external monitoring |

| Targets | Commitments | Monitoring arrangements |
|--|--|---|
| Integrated Manner | Implementation of fee systems for payment of ecosystem services | Regular review/assessment of implementation of fees system per countries |
| Target 7 – Pro-poor Innovative Financing | Letter of Commitment signed by key organisations in 6 countries where WSUP operates or IRC has close links | Review of targets and achievements published on IRC and WSUP's websites in September 2012 and annually till 2015. |



6. Conclusions

In conclusion, this Core Group has identified a number of key messages, as detailed below.

Access to water services and preservation of water resources requires adequate financing, in order to increase access to services, maintain service quality and realize the associated economic, social and environmental benefits. Overall funding to the sector needs to be increased, supported by strong political commitment to maintain levels of funding over time as long as water investments continue to demonstrate their value-for-money.

Governments and utilities should strategically plan ahead to ensure that the costs of preserving water resources and providing sustainable water and sanitation services are covered from an adequate mix of the 3Ts, i.e. revenues from tariffs, domestic taxes and transfers from external donors and philanthropic organisations. A pre-condition for sustainable financial flows to the sector is that water services are managed cost-effectively so that consumers, governments and investors have confidence that effective use is being made of financial resources. Only adequate and predictable flows of revenue from the 3Ts can leverage repayable financing from public and private sources (in the form of loans, bonds or equity).

Sufficient financial resources are needed to ensure the sustainable management of water resources. Financing for water service delivery and infrastructure for water supply and sanitation and agricultural requires financing water resources management and the environment for overall sustainability. Improved financing for agriculture water is necessary since it is the largest and most inefficient water consumer and necessary for food security.

There can be no right to water without sustainable cost-recovery, which is needed to ensure that water and sanitation services are delivered by viable and efficient public or private providers. Well-designed tariffs are crucial and should be set through transparent processes, taking account of local affordability levels and the local costs of providing services, with appropriate measures in place to ensure that the poor and vulnerable groups have access to sustainable and affordable services. Pro-poor financing mechanisms should be fostered to ensure the right to water is achieved universally in a sustainable and cost-effective way.

Strengthening the capacity of governments and utilities is a key condition to attract investment. This can be done through “soft measures” (such as to help strengthen project design or implement monitoring and evaluation systems for example), which need to be adequately financed. When responsibilities for water and sanitation are decentralized, local governments need to have adequate capacity, including financing, to deliver their functions.

Additional funding can be mobilized from new sources, such as decentralized cooperation, which transfers financial resources as well as technical know-how from local authorities in developed countries to local authorities in developing countries.

Grant funding should be targeted to those activities that can help leverage additional funding to the sector through the use of innovative financial mechanisms, such as Output-Based Aid and Progress Linked Financing. Such mechanisms can help ensure that spending is effective and can incentivise capacity development and institutional change.



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