

Questions & Answers: A Cost Comparison of Public and Private Water Utility Operation

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Several members of Congress, as well as the Obama administration, have recognized the need to improve our country’s valuable drinking water and wastewater systems. They are pursuing commendable policies, including reauthorization of the Clean Water Act and creation of a Clean Water Trust Fund, which will help improve water quality and protect waterways across the nation.

While working through the details of such legislation, it is important to ensure wise allocation of taxpayer money. Because of the underlying costs associated with private operation, the public should not subsidize for-profit water services. Below are common questions with answers that can help clarify why public money for public utilities is the best deal for taxpayers.

Q. Do private utilities charge more for water and sewer service?

A. Yes, compared to local governments, private utilities charge the typical household 33 percent more for water (see table 1) and 63 percent more for sewer service (see table 2). For several states, the difference is even starker. In Delaware, investor-owned utilities charge 75 percent more than municipalities do for water.¹ In Texas, American Water charges two and a half times as much as the typical municipality for sewer service.²

Q. Are private water utilities more efficient than public utilities?

A. No, private utilities are not more efficient than public utilities, according to a meta-analysis of 17 econometric studies about privatization and costs in water distribution by professors from the University of Barcelona and Cornell University.³⁹

Q. Does profit motive encourage private utilities to reduce costs?

A. No, in fact, profit motive can drive up costs. Because of state price regulation, private water utilities tie higher earnings to increased costs. They earn a rate of return on investment, so that the more they spend on a system, the more they profit.

Table 1. Comparison of Annual Household Water Bills of Public and Private Utilities By State(s)

State(s)	Annual Household Bill		Percent that Private Prices are Greater
	Municipal or Local Government Utility	Private or Investor Owned Utilities	
Alaska ³	\$441.84	\$458.79	4%
Arizona ⁴	\$225.00	\$329.40	46%
Arkansas ⁵	\$273.83	\$344.68	26%
California ⁶	\$415.86	\$500.42	20%
Connecticut ⁷	\$300.72	\$398.13	32%
Delaware ⁸	\$256.20	\$449.40	75%
Florida ⁹	\$300.96	\$360.02	20%
Illinois, Indiana, Iowa, Kansas, Michigan, Minnesota, Missouri, Nebraska, Ohio and Wisconsin ¹⁰	\$280.44	\$318.72	14%
Illinois ¹¹	\$240.84	\$326.88	36%
Indiana ¹²	\$232.68	\$318.81	37%
Iowa ¹³	\$219.84	\$314.16	43%
Kentucky ¹⁴	\$316.07	\$361.21	14%
Maryland ¹⁵	\$232.50	\$381.00	64%
Massachusetts ¹⁶	\$357.00	\$481.00	35%
Maine ¹⁷	\$331.31	\$362.81	10%
New Hampshire ¹⁸	\$411.70	\$582.00	41%
New Jersey ¹⁹	\$258.00	\$318.00	23%
New Mexico ²⁰	\$259.83	\$356.34	37%
North Carolina ²¹	\$204.12	\$344.76	69%
Ohio ²²	\$444.73	\$510.40	15%
Oregon ²³	\$271.79	\$313.97	16%
Pennsylvania, New Jersey, Maryland ²⁴	\$289.20	\$367.20	27%
Tennessee ²⁵	\$306.00	\$381.00	25%
Texas ²⁶	\$329.40	\$553.80	68%
Utah ²⁷	\$307.23	\$359.05	17%
West Virginia ²⁸	\$375.40	\$456.82	22%
Wisconsin ²⁹	\$252.03	\$400.55	59%
Wyoming ³⁰	\$261.83	\$343.00	31%
Average			33%

Table 2. Comparison of Annual Household Sewer Bills of Public and Private Utilities By State

State	Annual Household Bill		Percent that Private Prices are Greater
	Municipal or Local Government Utility	Private or Investor Owned Utility	
Alaska ³¹	\$348.00	\$625.13	80%
Arizona ³²	\$247.32	\$371.52	50%
Florida ³³	\$452.95	\$519.43	15%
Indiana ³⁴	\$371.16	\$493.56	33%
North Carolina ³⁵	\$285.36	\$567.12	99%
Ohio ³⁶	\$466.00	\$556.66	19%
Texas ³⁷	\$261.72	\$666.00	154%
West Virginia ³⁸	\$382.35	\$410.92	7%
Average			63%

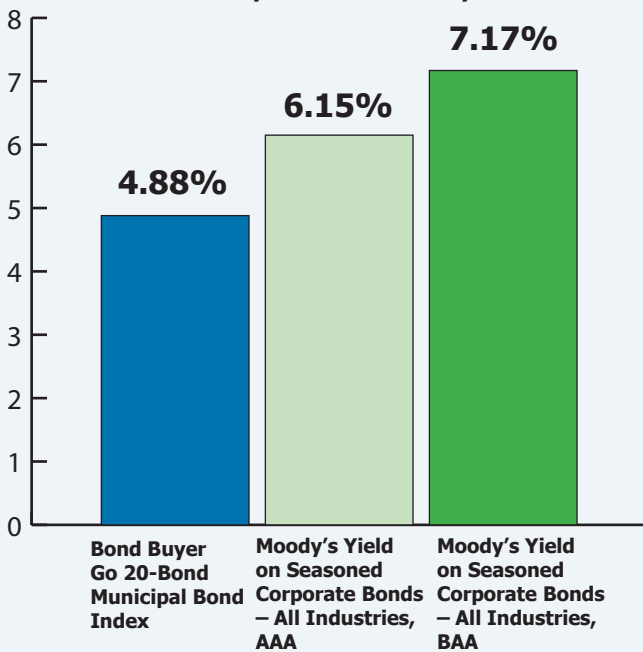
Q. Does privatization reduce the cost of water and sewer projects?

A. No, private management of water and sewer projects often increases costs. A professor of economics from Florida State University studied the construction of 35 wastewater treatment plants and concluded, “These figures suggest that choosing the privatization option is more costly than going with the traditional municipally owned and operated facility.”⁴⁰

Q. Does privatization reduce financing costs?

A. No, private financing generally is more expensive than public financing. For example, over the last decade, even the best-rated, or prime, corporate bonds were 26 percent more expensive than the typical municipal general obligation bond, and medium-grade corporate bonds were 47 percent more expensive than municipal bonds (see figure 1).⁴¹

Figure 1: Average Annual Interest Rates for Bonds Issued Between January 1999 and January 2009



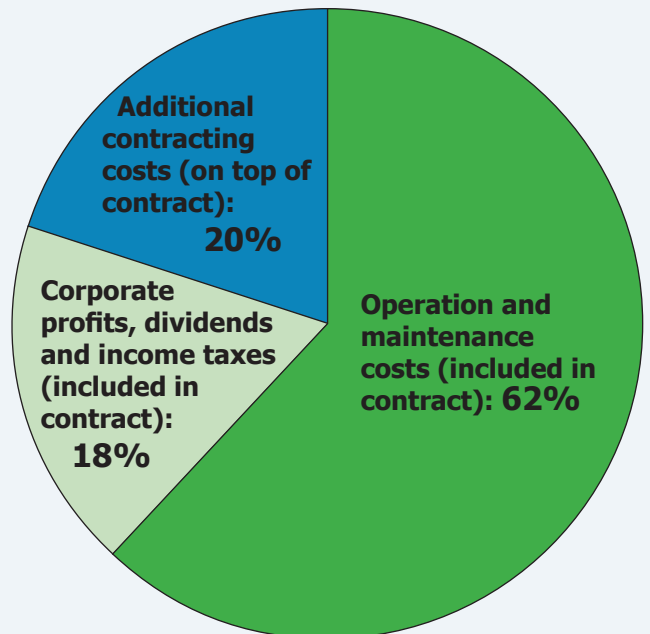
Note: Average of monthly releases from the Federal Reserve Board



Q. Does competition lead to cheaper contracts and reduced costs?

A. In theory, it would, but in practice, there is little to no competition for water service contracts. Without competition, the public has no room to negotiate and can get stuck with bad and expensive deals. One academic study found that the water market is “rarely competitive.”⁴² The nation’s massive infrastructure needs may only make this worse as water corporations consolidate for greater access to capital to finance improvement projects.⁴³

Figure 2: Total Cost of Water and Sewer Contracting



Profit requirements, income taxes, contract monitoring and administration and other contracting expenses can add more than 60 percent on to operation and maintenance costs.



Q. How much do profits and taxes affect the cost of water service?

A. In total, corporate profits, dividends and income taxes add 20 to 30 percent onto operation and maintenance costs (see figure 2).⁴⁴

Q. How much does it cost for a municipality to enter into a contract with a private operator?

A. In total, contract monitoring and administration, conversion of the workforce, unplanned work and use of public equipment and facilities can increase the price of a contract by as much as 25 percent (see figure 2).⁴⁵ Other hidden expenses, including change orders, cost overruns and termination fees, can further inflate the price of private service.

Q. What are the cost-cutting measures employed by private operators?

A. When private operators attempt to cut costs, they often use shoddy construction materials, ignore needed maintenance, and downsize the workforce, which impairs customer service. On average, more than one-third of water utility jobs are lost after privatization.⁴⁶ Such neglect hastens equipment breakdowns and increases replacement costs, which the public must pay for. In many contracts, private operators can technically comply with their contract terms while effectively shifting upkeep costs to the public.⁴⁷

Q. Do municipalities lose anything by contracting out water or sewer services?

A. Yes, public operation often has several additional benefits that municipalities can lose when they privatize services: revenue from government entrepreneurial sales

of services and products, including biosolids and wastewater effluent; intra-government coordination to pool resources and assist other government departments; and inter-government coordination to protect water resources, manage watersheds and work for long-term sustainability.⁴⁸

Q. Should the government give out low-interest loans to private water and sewer utilities?

A. No, it is illogical for taxpayers to subsidize investor-owned water utilities that regularly send profits out of local communities to stockholders in distant places. The federal government should invest in public utilities, which will reinvest the money into communities.

End Notes

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