

## TC ABSTRACT

### I. Basic project data

▪ Country/Region:	Regional
▪ TC Name:	Development of action plans of commercial areas and corporate governance, and supporting capital market access of water and sanitation utilities
▪ TC Number:	RG-T2601
▪ Team Leader/Members:	Lucio Garcia Merino (INE/WSA), Team Leader; Team members: Corinne Cathala, Keisuke Sasaki and Irene Cartin (INE/WSA); and Javier Jimenez (LEG/SGO)
▪ Indicate if: Operational Support, Client Support, or Research & Dissemination.	Research and Dissemination
▪ If Operational Support TC, give number and name of Operation Supported by the TC:	
▪ Reference to Request <sup>1</sup> : (IDB docs #)	
▪ Date of TC Abstract:	February 20, 2015
▪ Beneficiary (countries or entities which are the recipient of the technical assistance):	Water and sanitation operators in Latin America and the Caribbean region
▪ Executing Agency and contact name (Organization or entity responsible for executing the TC Program) {If Bank: Contracting entity} {If the same as Beneficiary, please indicate}	Bank executed (INE/WSA)
▪ IDB Funding Requested:	\$300.000
▪ Local counterpart funding, if any:	-0-
▪ Disbursement period (which includes execution period):	36 months
▪ Required start date:	March 15, 2015
▪ Types of consultants (firm or individual consultants):	Individual consultants
▪ Prepared by Unit:	INE/WSA
▪ Unit of Disbursement Responsibility:	INE/WSA
▪ Included in Country Strategy (y/n);	No
▪ TC included in CPD (y/n):	No
▪ GCI-9 Sector Priority:	Water and sanitation infrastructure

## II. OBJECTIVE AND JUSTIFICATION

- 2.1 In November 2014 the IDB approved a Water and Sanitation Sector Framework (the Sector Framework) to support the countries in the region in sustainably achieving universal coverage in water and sanitation (W&S) sector. The Sector Framework highlighted the necessity of addressing main challenges in the W&S sector, including inefficient service management, low private sector participation, and financial sustainability. In many countries inefficiencies<sup>2</sup> among firms have proven to be a major obstacle to effective service delivery and expansion, and is a substantial drain on local and national finances and, sometimes, on donor contributions. The large majority of water utilities in LAC display major shortcomings in their management and in financial and operational transparency.
- 2.2 One of the most important lessons learned from the sector reforms undertaken in the last two decades is the crucial role of governance as a determinant of the effectiveness of sector institutions and policies, and consequently as a condition for achieving widespread access to services and good quality and high efficiency of service delivery. This means that in order to support substantial and sustainable progress in terms of access, quality and efficiency through Bank operations, it is necessary to analyze governance structures and adapt operations (reforms) accordingly. The corporate governance of the W&S utilities is one critical element of the overall sector governance.
- 2.3 Efforts to enhance the efficiency of regional W&S operators are warranted. In 2010, at the request of various operators, the Water and Sanitation division of the IDB conducted the development of tools to assist operators of water companies in the identification and adoption of best practices in the areas of commercial management and corporate governance. The proposed tools help perform a review of these activities in a given company, and identify the areas and processes to be strengthened, as compared to industry standards and to derive an action plan. Developing an action plan should logically be the result of the implementation of the tool in a water supply company. With respect to corporate governance, the evaluation tool allows to identify (i) priority areas for sector reform and policy dialogue; and (ii) critical issues that may condition the success of loan operations. As a result of the use of the evaluation tool, water operators are able to develop action plans.
- 2.4 Meanwhile, the heavy investments required in the sector<sup>3</sup> (to achieve universal coverage by 2020 will require some US\$22 billion to be invested in safe drinking water and some US\$43 billion in improved sanitation. If these sums are coupled with the requirements for solid waste management, wastewater treatment and storm drainage, the financing needs double, not counting investments in quality improvement) call for a redoubling of efforts to give W&S utilities better access to credit and to capital markets. Its potential is substantial as many public utilities in the region (in big and smaller countries)<sup>4</sup> have low debt and are in a financial position to do this, especially in

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<sup>2</sup> A study from the Association of Water and Sanitation Regulatory Entities of the Americas, ADERASA, shows that, on average, 40% of all water supplied by companies goes uninvoiced.

<sup>3</sup> See Ducci et al. ([Drinking Water, Sanitation, and the Millennium Development Goals in Latin America and the Caribbean](#))

<sup>4</sup> See Ducci and Garcia ([Key financial indicators for water and sanitation utilities in Latin America](#))

- countries where the regulatory and institutional framework is more developed, as concluded by an analysis of more than 60 W&S operators in the region<sup>5</sup>. As W&S service providers shift from an engineering vision to a corporate service and commercial service vision, demand for better corporate governance, transparency, accountability, and efficiency in service delivery increases. This makes them more attractive to capital markets and financiers. Among the region's better performing utilities, there is a growing interest in diversifying its financial source, in particular, by accessing capital markets, and such utilities have manifested the needs for assistance in moving forward<sup>6</sup>.
- 2.5 Given the significant interest demonstrated by W&S operators in the region with respect to the two tools and thereafter making improvements, and also, given substantial potential for operators' access to capital markets, INE/WSA decided to support W&S utilities' preparation of action plans in the areas of commercial management and corporate governance, and activities required for facilitating their capital market access.
- 2.6 In 2011, the Bank approved a Technical Cooperation (ATN/OC-13096-RG) for the development of actions plans of commercial management and corporate governance activities in water utilities through the use of the corporate governance<sup>7</sup> and commercial management<sup>8</sup> evaluation tools, including developments of action plans based on the previous diagnosis. In this regard, the final outputs of this TC include more than 8 developments of actions plans of commercial management or corporate governance in several water utilities in the region. This new Technical Cooperation will continue the efforts initiated by the Bank with the previous TC.

### III. DESCRIPTION OF ACTIVITIES

- 3.1 The objectives of this Technical Cooperation operation are: (i) finance the contracting of individual experts to diagnose water utilities through the use of the corporate governance([Corporate Governance Technical Note](#), [Corporate Governance Tool](#)) and commercial management ([Commercial Management Technical Note](#), [Commercial Management Tool](#)) evaluation tools, and develop action plans based on the diagnosis;

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<sup>5</sup> [Idem](#)

<sup>6</sup> Utilities in Chile are a prime example: since their privatization, they have been accessing the securities market and have been issuing medium and long-term bonds in local currency, in this way financing more than 80% of their investments. This is also the case of some public utilities in Brazil and Colombia that have been able to access local and international capital markets (SABESP from São Paulo, for example, is traded on the New York Stock Exchange).

<sup>7</sup> The corporate governance tool contains a methodology to promote the use of good corporate governance practices for water and sanitation enterprises (especially SOEs) in Latin America and the Caribbean, based on IDB experiences and other relevant cases from network utilities. The methodology evaluates how corporate governance practices are currently being applied in those firms, and facilitates progressive advancement in successive stages. The methodology is rooted in theory in order to ensure that the governance of water and sanitation enterprises contributes to the efficient and sustainable use of resources, so that the social investment in water and sanitation in the region may play a part in the achievement of the Millennium Development Goals

<sup>8</sup> The commercial management tool evaluates customer management practices in use by water and sewerage utilities. In order to facilitate the use of this tool, all matters which relate to customer management have been grouped into four main functional areas: the "Billing Factory" (or the recurrent billing and collection activities); Revenue Management; Customer Care (management of contacts with customers); and Customer Marketing, a relatively new activity in water and sewerage companies, which aims to study and propose solutions tailored for various types of customers.

and (ii) finance activities required for facilitating W&S utilities' capital market access. This operation will comprise 2 components as follows:

- 3.2 **Component 1:** this component will finance the contracting of individual experts in commercial management and corporate governance to advise water utilities regarding the use of the evaluation tools. These experts may prepare the diagnosis report themselves or assist the operators with its preparation. These experts will also assist the water operators with the establishment of their action plans, and documentation needed to be presented to the Bank for financing either through projects in preparation or execution and/or technical cooperation operations. It is estimated that around 10 diagnosis and action plans in commercial management or corporate governance activities will be developed.
- 3.3 **Component 2:** this component will finance priority activities required for facilitating W&S utilities' capital market access. Activities may include hiring of IPO advisory, investor relationship advisory, debt sustainability analyses and rating services, as well as institutional strengthening in relevant areas, such as accounting and disclosure, financial management, internal control, and business planning. This component may also include development of knowledge products by the division that assists W&S utilities in preparing for capital market access (e.g. case studies, best practices and toolkits).

BUDGET				
Activity/ component	Description	IDB funding (US\$)	Counterpart funding (US\$)	Total funding
<b>Component 1</b>				
Experts in commercial management	Preparation of diagnosis, action plans, and loan requests for water utilities	125,000	0	125,000
Experts in corporate governance	Preparation of diagnosis, action plans, and loan requests for water utilities	100,000	0	100,000
<b>Component 2</b>				
Capital market access	Priority activities to facilitate W&S utilities' capital market access; and development of knowledge products	75,000	0	75,000
<b>Total funding</b>				<b>300,000</b>

#### IV. EXECUTING AGENCY AND EXECUTION STRUCTURE

- 4.1 The Bank (INE/WSA) will execute this technical cooperation operation. According to Appendix 10 –Criteria Contracting Bank GN-2629-1 policy, the execution by INE/WSA is justified because it will be used as operational support for project preparation and support of projects execution in the region. INE/WSA will be responsible for all aspects of this technical cooperation, including disbursements.

## **V. PROJECT RISKS AND ISSUES**

- 5.1 Project risks may include the implementation by the utilities of the activities recommended in the action plans in commercial management and corporate governance activities developed with this technical cooperation (for example, procurement of new billing systems, integration of commercial and financial systems, development of a code of ethics, among others activities) . The Bank will monitor closely the implementation of these actions plans, and may include resources in the loans (during preparation or execution phase) for this implementation.

## **VI. ENVIRONMENTAL AND SOCIAL CLASSIFICATION**

- 6.1 Given that the nature of the activities to be financed by the technical cooperation, it is expected that no negative environmental and social impact will result from this operation. This TC has been classified as a C operation as assigned by ESG.