Public Private Partnership as a Policy Dilemma

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Abstract: This paper has three objectives: first, to acknowledge the basic right to water as recently recognized by the UN and, consequently, to address the government’s responsibility to provide water services; second, to describe the problems and dilemma in the privatization of water services in Jakarta, the capital city of Indonesia, as a policy choice; third, to reinforce the idea that privatization of public services is beneficial but not a panacea; therefore, the government as the center of public administration needs to reconsider some of their key policies on public services.

Keyword: public policy, privatization, water, government.

INTRODUCTION

Indonesia is a country of more than 2,500 islands, and Jakarta, the capital, is located on the Java Island, one of the big five Indonesian Islands. Today Indonesian population is estimated to be 234.2 million, compared to 205.1 millions in 2000. Indonesia is now the fourth most populated country in the world, after China (1.33 billion), India (1.16 billion), and the US (309.2 millions). In 2010, 60.1% of the population, i.e. about 121 million people, lived in Java, making it the most densely populated island (103 people per km²) in Indonesia. In 2009, the Indonesian GDP per capita was US$ 2,590.

Jakarta covers an area of 661.52 km² with a population of 8,522,589. It is the most densely populated city in Indonesia, with about 12,883 people per km². Administratively, Jakarta comprises of five districts: North Jakarta, East Jakarta, West Jakarta, South Jakarta, Central Jakarta, and the Thousand Islands Municipality. In 2009, the GDP per capita in Jakarta was USD 8,400 or 320% of the Indonesian GDP per capita. This was due to 70% of money in Indonesia circulating in Jakarta, thus attracting the biggest number of business activities.

Trade and services contribute about 71.5% to the regional GDP. Jakarta has a mission of becoming The Service City, or a city that provides world-class service. To achieve this, Jakarta must be able to accomplish the Millennium Development Goals, a pledge made in an International Summit in New York in 2008. One of the criteria is 80% of the population must have clean water delivered via pipes. More importantly, the delivery of water via pipes ensures that groundwater will not be used, thus preserving the land and avoiding the use of polluted groundwater.

Indonesia has adopted the idea of the “basic right to water” since its independence. The Indonesia’s 1945 Constitution Article 33 states: “The land, the waters, and the natural resources within shall be under the powers of the State and shall be used to the greatest benefit of the people.”

The statement “under the powers of the State” does not mean all activities should be managed only by the government. Natural resources may, to a certain extent, be managed by the private sector, communities, or corporations, and supervised by the government. This includes land and water with economic value and social functions. The utilization must be carried out in a sustainable manner and for the prosperity of the Indonesian people (Nugroho, et.al, 2009). Therefore water service providers, called Perusahaan Daerah Pelayanan Air Minum (PD PAM or PAM), are established on the local government level. These are regional water service companies with a local government-owned enterprise (LGOE) status. PAM Jaya as the local LGOE provides clean water for the public.

Law No. 7/2004 on Water Resources stipulates that water resources must be managed based on the principle of conservation, balance, public benefit, integrity

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1 The big five Indonesian islands are: Papua, Kalimantan, Sumatera, Sulawesi, and Java, with Java as the most urban and densely populated island. More than 50% of the total population (270 million) lives in Java.
3 Indonesian Central Bureau of Statistics, February 2010. This was a tremendous turnaround. In 1999, after Indonesia was hit by the financial crises, the GDP per capita was about USD 400. In 1996, the GDP per capita rose to USD 1,050.
5 As opposed to State Owned Enterprises (SOEs)
and harmony, justice, and independence, as well as transparency and accountability. According to this principal law in water resources, a river area refers to integrated water resources management in one or more watersheds and/or small islands with an area of less than or equal to 2,000 km². The above stipulation applies to river areas in one regency/municipality, inter-regency/municipality river areas, inter-provincial river areas, transnational river areas, and nationally strategic river area. (Nugroho, et.al, 2009). The policy serves as the basis for the practice of regional government cooperation in managing cross-border water resources.

There are two levels of policies in water service management. At the national level, the central government sets the standards for water service, its quality and price structure. At the regional level, the local government establishes regional companies exclusively owned by the local government to produce and distribute clean water. The policy is mostly implemented in cities, but rarely on the district level. A city or kota in Indonesian refers to an administrative urban area which consists of several kelurahan (sub-districts), and the district level refers to an administrative rural area which consists of desa (Villages). Therefore, every city in Indonesia must have one water company owned and managed by the government. The reason is that the government is obliged to provide water service to people, thus water is a public service, not a commercial product.

When the population increases, especially in urban areas, the local government is unable to provide clean water management. Less than 10% of PAMs do their job well, as most of them face three problems. First, their profit is low because local governments tend to see clean water as a political commodity. In order to remain popular with the public and maintain their power, local authorities keep the water bills low without providing subsidies for them, as subsidies would have to be paid for with the local budget. Water companies thus suffer from financial problems and often lose their investment sources, because banks and other loan institutions are unwilling to give them financial support. Second, local politicians and bureaucracy often interfere with the management in water companies. Members of the water company’s board of directors and commissioners are elected by local politicians. The members’ position in the top management is determined by their loyalty to local politicians. Therefore, the real customers are not the public who consume and pay for the water bill, but those politicians. This leads to the third problem: poor management in water service companies.

All three problems are present in PAM Jaya in Jakarta. Their financial performance is lacking, as are their technical and professional ones. Insolvency and poor management have led PAM Jaya into the idea of privatization of water services. The objective is clear: to increase the technical and service quality in water provision. Pressure from the central government and firm advice from the World Bank resulted in a policy: the privatization of water service in Jakarta for 25 years under the Public Private Partnership (PPP) scheme. Public policy is the choice made by the government whether or not they would implement it (Dye, 1995). Jakarta has chosen privatization in order to provide clean water to the public.

There are some disputes about the basic principle of PPP, about whether or not it is privatization. To my understanding, PPP is a type of privatization (Sanjoyo and Nugroho, 2006). Even the broadest meaning of PPP includes the involvement of non-government institutions in carrying out the government’s job (Yescombe, 2007); business sectors and non-profit organizations are both involved in government activities. Indeed, it is not easy to distinguish between PPP and non-PPP, since public administration in democratic countries involve their stakeholders in government decisions and practices, and business and non-profit organizations are constituents of democracy.

PPP is the private sector’s involvement in public infrastructure; the latter is defined as the facilities required for the economy and society to function (Yescombe, 2007). Disagreements about the definition of PPP notwithstanding, it constitutes of at least four crucial aspects. First, the sale of public assets, including the denationalization of public corporations and the sale of publicly owned land and buildings. Second is charging; this refers to the privatization of the financial costs of a service which is still provided by the public sector. Third is contracting out, which refers to the privatization of the production of a service by means of substituting private contractors for in-house employees, although the service continues to be financed by the public sector. Fourth is liberalization, which is referred to as deregulation. This involves the reduction or removal of statutory monopoly provisions, which have prevented private firms from entering public sector markets (Braddon and Foster, 1999). Privatization takes one of two principal forms. The first is simply the sale or transfer of state-owned enterprises (SOEs) to private sector units. The second is contracting out a service originally provided by a government institution to a private company. From these meanings we can see that PPP is a privatization.

PPP is a form of privatization, since in its basic principle the strategic government’s accountability toward public

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6 There are two performance indicators that PPP should aim toward, namely the technical target and service target.
services is being transferred to parties other than the
government. These can be business corporations or non-
profit organizations or other organizations. The transfer
is done by contracting out, concession, or divestment.
However, the government still has power, being the
highest-ranking political body in the social and political
system where the accountability is transferred to the other,
lower-ranking party. The power includes tangible objects
such as assets and intangible ones as such services; the
transfer includes transfer of ownership (divestment) and
time of ownership (concession). The idea to separate PPP
from privatization seems like an academic one, although
in truth it is politically motivated.

PPP is favored by many: governments, the business
sector, and international financial organizations. Their
reasoning is that PPP is an alternative where government
services may be provided without being funded by taxes
(see Yescombe, 2007). PPP policies aim to reduce the role
and scope of the public sector, whilst encouraging private
sector involvement in the gap left; to create, by legislative
or regulatory means, new opportunities for private
expansion into traditional areas of the public sector; to
attract private sector investment and involvement to
support government policies; and to promote competition
by increasing market pressure on assets remaining within
public sector (Braddon and Foster, 1999).

PPP as privatization had its own private wars.
Hodge describes the three wars within privatization:
philosophical, practice, and humanity. First, it is a part
of a philosophical battle where individualism is preferred
over collectivism. In collectivism, the collective good is
prioritized over one’s own individual private interests. The
collective good is the lifeblood in the role of government
which has been transferred to the private sector. The
second is war regarding service delivery; the question of
which one is better situated to deliver government
services, the public or private sector is best placed. The
third war in privatization exists in the eternal struggle
of capital interest against civility in society and human
rights (Hodge, 2006).

Philosophically speaking, privatization also means a
wars on ethics. According to Buttle, privatization should
also be regarded in ethical terms concerned with the
pursuit of moral objectives and, therefore, appraised in
moral, as well as economic and political, terms (Buttle,
1999). In Buttle’s point of view, PPP disregards the moral
objectives that should be met by any privatization policy
choice. There are two ways in which privatization concerns
moral objectives. First, underpinning privatization is the
vision of a good society, a society which is desirable,
which ought to be achieved, which has more value
than alternative types of society. Second, underpinning
privatization is a vision of a good person, the sort of
person who is considered as morally admirable, whose
life is thought to be of value and worth (Buttle, 1999). It
is about value and actor.

In practice, PPP results in several serious failures7.
In water service privatization through PPP, over 30 PPP
water contracts in global major cities - from Africa,
Europe, to South America - have been terminated and
restated (Hall, 2010). Franceys and Gerlach discovered
that PPP international investors hesitate to invest due
to the high level of uncertainty in developing countries
(Franceys and Gerlach, 2008).

In regard to humanity, PPP is facing political and
ethical problems. In business and markets, monopoly
is not a beneficial concept. Therefore, only government
institutions are allowed to do monopoly. In PPP,
government monopoly is changed into private monopoly.
Public monopolies that have become private monopolies
are unresponsive to the consumers’ wishes (Buttle, 1999).
The ethical dilemma in business theory does not stop here.
The next issue is political: PPP, as part of the privatization
policy, becomes a fraudster. The shift of enterprises
from the public to the private sector does not result in
individuals as consumers or shareholders being able to
exercise more control over the institutions that influence
their lives than was the case with enterprises that were
part of the public sector. Privatization, then, results in
an impoverishment of democracy and leaves large areas
of society’s affairs beyond democratic influence (Buttle,
1999).

Jakarta has had a modern water supply system since the
Dutch colonial times in the 1940s. After the Indonesian
independence in 1945, the service is managed by the
local government-owned company (LGOC), Perusahaan
Daerah Pelayanan Air Minum Jakarta Raya8 (PD PAM
Jaya). The company is Jakarta’s means of developing a
pipe water supply system with extensive coverage area
for the metropolis. The idea is that the use of groundwater
will be reduced significantly for two reasons: to protect
Jakarta from land subsidence, and to guarantee water
quality service for the public. This can be achieved
because groundwater is not used as a primary water
resource by the city residents.

In 1996, the company experienced serious problems
in service improvement due to financial and management
issues. At the same time, the World Bank introduced
the idea of privatization of public service as Public
Private Partnership (PPP). These factors resulted in an

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8 Perusahaan Daerah Pelayanan Air Minum Jakarta Raya = Regional
Company for Water Service Provision in Jakarta.
agreement in 1998 between the DKI Jakarta Government, represented by PD PAM Jaya, with two private investors: Thames of the UK and Suez of France. Both investors had local partners.

The policy began with President Soeharto’s instruction on the importance of the PPP scheme. The Letter of Intent was later signed by the Minister of Public Works and the DKI Jakarta Government, and incorporated into the Minister of Public Works Decree No. 249/KPTS/1995, dated July 1995, and the DKI Governor Decree No. 1327/95, dated October 31, 1995. On October 6, 1995, letters of appointment for private operators for the management of clean water provision in DKI Jakarta were issued. The project is divided into two service areas, namely the west and east sides of the Ciliwung River. Next, letters of invitation were issued to two prospective drinking water operators, both international companies, namely Thames Water (partnering with PT Kekar Pola Airindo (PT KPA)) on June 30, 1995, and Lyonnaise des Eaux, presently Suez Environment (partnering with PT Garuda Dipta Semesta-PT GDS), on August 21, 1995. Each operator later submitted its response to the Minister of Public Works, stating their readiness to complete the Feasibility Study (FS) within six months. On October 6, 1995 a MoU was signed. Among others, it states that concession on one part of Jakarta is awarded to Thames and PT Kekar Pola Airindo, a company owned by Soeharto’s son, whereas the other part is awarded to Lyonnaise des Eaux and PT Garuda Dipta Semesta. The negotiation process lasted for two long years, involving prominent institutions such as the World Bank/IBRD, Ministry of Public Works, Bappenas, Ministry of Finance, and Provincial Government of DKI Jakarta (Lanti et al., 2009).

The May 1998 riot and the fall of Soeharto brought about a major change. The economic climate was no longer profitable for the crones and business network of the former President Soeharto. Following the social unrest and reformation, the Suez and Thames directors realized that the recently signed concession contract has lost its political support. Their partner, who was previously going to help them overcome the bureaucratic obstacles, has suddenly become a burden that hinders the effectiveness of the cooperation agreement (RCA). In fact, the Provincial Government of DKI Jakarta issued a policy that no longer supported private consortia. Therefore the foreign companies must formulate a new strategy in response to the changing situation. The executives of the drinking water operator also realized that re-negotiation of the cooperation agreement could no longer be avoided. The re-negotiation, however, did not proceed as smoothly as expected (Lanti et al., 2009).

The Restated Cooperation Agreement (RCA) was finalized and signed on October 22, 2001. In accordance to the RCA, the operators’ performance is measured with indicators in the technical target and service target standards. They are number of customer/connection, production capacity, service coverage ratio, volume of water sold, water-loss or unaccounted for water (UfW). Thus far there have been changes in ownership. 12 years ago, in 1997, the privatization of water services in Jakarta began. Before 1997, the water service provider was a local government-owned enterprise, PAM Jaya. In 1997, the concession of the west area was granted to PAM LYONNAISE JAYA, a Suez (formerly Ondeo Service) subsidiary company. Prior to July 2006, the private provider company was owned by Suez Environment (majority of shares), PT. Kekar Pola, and PT. Bangun Tjipta Sarana. After July 2006, it was owned by Suez Environment (majority), PT Astratel Nusantara (Astra International subsidiary, majority owned by Jardine Fleming), and Citigroup Financial Products. In the east area, prior to 2007, the concessionaire was PT Thames PAM Jaya, owned by Thames of UK (majority) and PT. Tera Meta Phora. Since 2007, Acuatico Pte. Ltd (majority) and PT. Alberta Utilities have taken over the company9. Despite these changes in ownership, the performance indicators still apply, and some of the performances remain good.

Palyja has been able to increase its connection number almost twofold compared to the pre-PPP era, from 209,895 connections in 1998 to 414,930 connections in June 2010. Aetra/TPJ has increased its connection number almost twofold compared to the pre-PPP era, from 278,083 connections in 1998 to 383,455 connections in June 2010. Palyja water production has increased from 150.4 M m³ in 1998 to 161.1 M m³ in 2009. Aetra/TPJ water production has increased from 245.9 M m³ in 1998 to 261.8 M m³ in 2009. Palyja Service Coverage Ratio has increased from 33.18% in 1998 to 64.09% in June 2010. Meanwhile, Aetra/TPJ Coverage Ratio has increased from 30% in 1998 to 59.65% in 2009. The total volume of water sold by Palyja in 1998 was 89.1 M m³, and it increased to 137.7 M m³ in 2009. Meanwhile, Aetra water sold in 1998 was 105.2 M m³, and it increased to 128.1 M m³ in 2009. The critical indicator for water services is called water-loss. In 1998, water-loss in Palyja concession was 58.63%, and it was reduced to 44.34% in 2009. In the first semester of 2010 it was reduced to 43.14%. Meanwhile, water-loss in Aetra/TPJ concession was 61.30%, and it was reduced to 51.07% in 2009. In the first semester of 2010 it was reduced to 50.45%.

At a glance, everything goes smoothly and the performance is good. However, there are still problems and conflicts in public water service in Jakarta today. The reason is that privatization of water is plagued by dilemmas.

The first dilemma is **whether or not water should be privatized.** According to the World Bank, “Bureaucrats typically perform poorly in business, not because they are incompetent (they aren’t), but because they face contradictory goals and perverse incentives that can distract and discourage even very able and dedicated public servants. The problem is not the people but the system, not bureaucrats per se, but the situations they find themselves in, these bureaucrats in business” (The World Bank, 1996).

Before the privatization, water service was managed by a government-owned company, PAM Jaya. The top management consisted of political appointees from the local polity and bureaucracy. Rather than serve the public, they tend to serve the polity and bureaucracy, since their performance and existence depend upon their ability to please the local polity and bureaucracy. Therefore, the government’s specific purpose vehicle (SPV) in providing public water service failed. The reason was more than mismanagement, it was lack of management. Abuse of corporate powers occurred frequently. Hence, bureaucracy must not be involved in services that are managed like a business, such as water service. Privatization was then assumed to be a magical solution for undermanaged corporations, financial problems, and a demand for fast improvement in water services.

The value of privatization does not merely concern a good society, but also concerns the way the government distances itself from its obligation as the primary actor in providing clean water for the public. The actor is a businessperson closely linked to power. The combination thus creates forced privatization.

The second problem is performance, or more specifically, technical performance. The two concessionaires have improved the service, but it is still a far cry from what the 25-year concession contract has promised. The treated water quality has never reached drinking water standards (potable), water loss is still high (45%), water tariff has increased sharply (the highest in Asia), namely

### Table 1. Target and Actual Performance of Water Service in Jakarta

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<td>1998</td>
<td>58.35 %</td>
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<td>1999</td>
<td>54.79 %</td>
<td>57.94 %</td>
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<td>2000</td>
<td>48.51 %</td>
<td>50.94 %</td>
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<td>- 2.43%</td>
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<td>2001</td>
<td>47.15 %</td>
<td>50.78 %</td>
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<td>- 3.63%</td>
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<td>2002</td>
<td>45.38 %</td>
<td>47.75 %</td>
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<td>2003</td>
<td>43.50 %</td>
<td>44.65 %</td>
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<td>- 1.76% (- 0.61%)</td>
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<td>2004</td>
<td>41.63 %</td>
<td>43.34 %</td>
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<td>- 6.18% (- 4.47%)</td>
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<td>2005</td>
<td>39.76 %</td>
<td>41.75 %</td>
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<td>- 10.60% (- 8.61%)</td>
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<td>2006</td>
<td>37.89 %</td>
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<td>- 13.28% (- 11.31%)</td>
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<td>2007</td>
<td>36.02 %</td>
<td>37.99 %</td>
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<td>- 14.99% (- 13.02%)</td>
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<td>2008</td>
<td>35.06 %</td>
<td>36.92 %</td>
<td>48.25 %</td>
<td>- 15.14% (- 13.28%) (- 1.95%)</td>
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<td>2009</td>
<td>34.11 %</td>
<td>35.56 %</td>
<td>47.15 %</td>
<td>- 12.74% (- 11.29%) 0.30%</td>
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<td>2010</td>
<td>33.15 %</td>
<td>34.18 %</td>
<td>46.05 %</td>
<td>- 13.24% (- 34.18%) 0.34%</td>
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<tr>
<td>2011</td>
<td>32.19 %</td>
<td>32.77 %</td>
<td>44.52 %</td>
<td>- 11.31% (- 10.73%) 1.02%</td>
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<td>2012</td>
<td>31.23 %</td>
<td>31.21 %</td>
<td>43.25 %</td>
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<td>2013</td>
<td>30.28 %</td>
<td>30.00 %</td>
<td>41.62 %</td>
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<td>2014</td>
<td>29.32 %</td>
<td>28.68 %</td>
<td>40.00 %</td>
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<td>2015</td>
<td>28.36 %</td>
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Source: Jakarta Water Regulatory Body, 2011
USD 0.7/m³ per January 2009, and about 64,500 customers (8.45% from the total number of customers) reported of having no water, and yet many are still billed. In 2003 (the first rebasing) and 2008 (the second rebasing), the water loss were below the target. The non-performance in water loss management is solved not by performance increase, but by lowering the water loss target so that it closely matches the result. Water-loss is the most the critical indicator for water service. Therefore, if the water-loss target is not achieved, the rest of the service is in danger of failing.

Private operators claimed that the service coverage ratio is 63.58%, so 3.2 million people are not served. The problem lies on the private operators’ assumptions that one connection serves seven people. JWRB ratio assumption is 1:4. The service coverage ratio is about 42%, meaning that more than half of the Jakarta population uses groundwater. To sum up, due to the low pipe-water coverage, households in Jakarta prefer groundwater as their primary water source.

The political problem concerns democracy. According to Buttle (1999), privatization goes against democratic values precisely because it removes important issues from public determination, and the decisions will reflect the directors and managers on behalf of the individual and institutional shareholders. This is indeed the case with water bills. Water privatization in Jakarta is essentially a performance-based contract, but the performance target is stated as indicative. The full-cost recovery contract leads to the “financial requirement of the private partners.” The internal rate of return (IRR) is not clearly stated; it is stated only in the feasibility study, pegged at 22%. The “technical assistance” fee, which is not unlike royalty, is levied. Water charge increases every semester regardless of the performance.

The contract defines two financial instruments: First, water charge, which is a specific amount of money charged by private operators to the PAM Jaya. It increases every semester regardless of performance. Second, water bills, set by the local government and proposed by the Jakarta Water Supply Regulatory Body (JWSRB). The bills are based on service performance, affordability, and the appropriateness of the business: for instance, an efficient business process. When the contract is signed, it is assumed that water charge must be lower than water bills. As such, there must be a margin that can be counted as profit for PAM Jaya on behalf of the Jakarta Government. This is called a revised PPP model, because usually in a PPP contract the concessionaire has the mandate to set the service fees that the user/public must pay for.

There would be no problem if service performance, efficient business process, and affordability are taken into consideration. Unfortunately, that is not the case. Unsound performance, inefficient business process, and fees beyond people’s affordability to pay, combine perfectly to hinder the two financial instruments in the contract. Water bills increase excessively every semester. What follows is inevitable: a shortfall or a huge negative profit.

From 2005 to 2009, the performances of both operators were below target. Therefore JWRB has not proposed tariff increase to the city government. PAM Jaya’s loan to the private operators for the last three years has increased from IDR 480 billion to IDR 552 billion due to the lack of tariff increase. Due to privatization, the government owes the private sector a huge debt. Jakarta can never provide water service for the poor, since every connection to poor people creates a new shortfall; the reason is that the water bills for the poor are far below the water charge.

In short, privatization has a hidden caveat: the private sector must profit in order to maintain the business and therefore the service. Privatization causes Jakarta to become the capital city with the highest water bills in Asia. The PPP’s promise of creating a “safe” government budget (Yescombe, 2007) is yet to be proven.

The Jakarta PPP policy faces two dilemmas. First, the government’s ethics. The question is: is it right that the government transfers water service accountability to the private sector or is it wrong? The government’s ethical principles concerning public rights should be clear. If the government is accountable for the rights, PPP must be terminated. This will result in three problems: It is unclear who will manage and fund the service, since the government has limited management and budget. PPP termination also entails a huge penalty for the government.

10 In February 2010, on a field visit to Muara Baru, North Jakarta, I found many poor customers who have had no water for 7 years but are still billed. The finding has been made into a documentary movie called “Seven Years without Water,” JWRB, 2010.

11 In 2007-2008 it was discovered that about 63.33% of Jakarta residents use groundwater wheel, both open and closed, and electric pumps. The research was conducted by Indonesian People’s Forum of Drinking Water Quality Management (Forum Masyarakat Pengelola Kualitas Air Minum Indonesia/Forkami) with 2,514 respondents in the five districts in DKI Jakarta.


13 The full cost recovery approach to water was discarded at the World Water Forum in Istanbul, Turkey, 2006, and replaced by sustainable cost recovery as developed by Camdebus Panel, initiated in 2003.

14 Mauritius Napitupulu, CEO PAM Jaya, Kompas, August 11, 2010.

15 The water bill is IDR 1,050 per m³, whereas the water charge is IDR 7,000. No one wants to pay for the shortfall.

16 The highest consumer charge is IDR (Rupiah) 12,000 per m³ (USD 1.3/ m³). Special prices for special customers according to the Jakarta Port Authority are: IDR 14,650 (USD 1.61), Singapore (USD 0.31 – USD 1.38), Kuala Lumpur (USD 0.14 – USD 1.27), Hong Kong (USD 0.55 – USD 1.19), and Taipei (USD 0.16 – USD 0.24) (Ali, 2010).
the total estimation of which is IDR 8 trillion; it is also unclear who will pay this penalty. Foreign investment termination may easily be read as a sign that global foreign investment in Indonesia is unhealthy. If PPP is continued, so will the following: the shortfall, highest water tariff in Asia, no service for poor, and other unsound performances.

The second dilemma is the PPP practice. The core idea of PPP is to transfer government financing for public infrastructure to the private sector. Water infrastructure investment is a risky business and required to be a long-term investment in order for the water tariff to remain affordable for the public. If the depreciation of the water treatment plant is assumed to take 40 years, the payback period is then assumed to be 25 years. Being a long-term investment, it also needs long-term financing. Financial institutions only provide short- and medium-term loans (one to five years) for private businesses. Therefore the 25 years of payback period must be shortened into, for instance, 5 years, and as a result the return must be extremely high. This means higher water tariff for the public, even when the service is poor. This is the first problem. The second problem is that the highest achievement in a private business means a sustainable revenue increase. Therefore, the water tariff will continue to increase even after the 5-year payback period is over and the revenue will come from the excessive tariff increase paid by the public (see figure 1). The dilemma here is that the only institution eligible for a soft-loan term (lasting 25 years or more) is the government. In regard to financing issues in public service infrastructure, the problem is not the transfer of government accountability to the private sector, but how to improve the governance of the government’s loan management.

Proposing that most the capital-intensive PPP in privatization is characterized by long investment payback periods. These are infrastructure investments, such as in telecommunication, energy, transportation, and water. They are the favorites of the private sector since they generate increasing shares of privatization revenues. This finding is in line with Yescombe’s (2007) premise that, while project finance loans in general have long repayment terms - about 15 to 20 years - most PPP project cash flows require the debt service to be spread out over 20 years or longer to match the natural life of the project and produce an affordable cost for Public Authority. PPP projects offer a high level of certainty in relation to long-term cash flows, and therefore provide a good basis for investment appraisal.
for long-term loans. Typically, when a new PPP market opens up, the loan terms grow shorter and lengthen as the lenders grow used to the risk involved. Another factor which determines the length of a loan is the lenders’ Cover Ratio requirements - the shorter the loan, the higher the debt service payments, and so the lower the Cover Ratio becomes. Paradoxically, the longer term a loan has, the safer it appears. Therefore it is clear that the long term in a loan for a PPP project can be misleading. Most commercial banks have short-term deposits, so long-term loans lead to a mismatch. Despite this, banks are prepared to provide long-term loans for PPP projects as a large proportion of PPP loans are refinanced after the end of the construction period (Buttle, 1999). According to Butlett, developing countries may not have commercial lenders willing to provide long term loans. Thus, in countries such as Brazil, where banks can earn a high return from short-term lending, there would be no good reason for them to divert funds to long-term loans, whether for PPP projects or anything else. Therefore in such cases, other sources of finance will have to be found. (Buttle, 1999)

**CONCLUSION**

Jakarta water privatization has clearly demonstrated the failure of PPP in water service. The government has the right objectives, but they are failed by the basic assumptions and policies developed. There are five incorrect basic assumptions. First, the government assumes that water service is not its responsibility, and therefore is not a primary government obligation. It can be easily transferred to the private sector and privatized in a PPP. Clean water service is a monopolistic public service, therefore transferring the service into the hands of the private sector means transferring public monopoly to the private. This violates the first law in business ethics. Water service is the highest priority for all city governments. The government has clear obligation and accountability, if not actually is the most accountable and obliged institution. The best water service at a minimum cost to meet public needs must be guaranteed. This can be managed by way of a public or government investment funded by taxes, as part of public service.

Secondly, it is assumed that the right to water is not part of human rights. However, this right has been acknowledged by the United Nations General Assembly when they voted unanimously to adopt a resolution recognizing the human right to water and sanitation on July 29.

Thirdly, the government assumes that PPP in water service is the same as in other infrastructure PPPs. PPPs in Kuala Lumpur and Singapore have succeeded because the cities use a different approach in water service compared to toll roads, ports, and telecommunication. The governments play the role not only of tariff setters, but also that of investors and guarantors of quality.

The fourth incorrect assumption is that the private sector is a savior angel. There is no such thing among business players; everyone is an agent in the economy, and the private sector has its own interests. It is assumed that private businesses are driven by the principle of efficiency and provide the best service at the lowest price. In practice, private businesses are more driven by the desire for profit than by efficiency. Privilege abuse by private businesses may occur whenever an opportunity is present. Without specific clauses in the business contract, performance and efficiency may be neglected. Furthermore, through PPP, the government legalizes monopoly by the private sector.

The fifth assumption is that PAM Jaya as a LGOE has failed to fulfill its obligations, and the reason for the efficiency is the government ownership in the institution. The solution is to transfer the business from the state-owned company to private business through the PPP. The fact is that PAM has failed due to a heavy intervention from the political and bureaucratic arenas. The main issue is professionalization, not privatization.

The lesson here is that PPP is a solution, not a panacea. PPP is important as a method, especially in water service. Water is a basic human right; therefore if PPP transforms public monopoly into private monopoly, its practices might reduce the values of democracy, public ethics, and the principal law of market efficiency. These values are promoted by Adam Smith in his classic work, *The Wealth of Nations* (1776), where he states that the private sector may not be granted monopoly, as the market is the only mechanism with the “hidden hand” to create business efficiency. Hence, the failure of PPP in the Jakarta Water Service is caused by a combination of four types of policy failures: management failure, meaning the policy is successfully formulated, but the actors are unable to implement it; administrative failure, meaning the policy is successfully formulated, but the implementation is costly; design failure, meaning the policy is successfully formulated, the implementation is successful, but the result is not according to the design; and theory failure, meaning the policy is successfully formulated, the implementation is successful and according to the design, but the results are not as hoped for because the policy assumptions were incorrect (Patton and Savicky, 1993).

Therefore, in regard to water service, a new policy framework is required. This is the case with a great many developing nations experiencing economic crises today, though the reason is not that they have taken the

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17 From a discussion with Phillip Marin, Bonn, December 3, 2009.
wrong steps. Rather, they are doing the right thing at the wrong time (Fairbanks and Lindsay, 1997). Thus we may consider changes for the policy framework: (1) From privatization of public enterprise to professionalization. (2) From public-private partnership to public-to-public-partnership19. (3) From government regulation to government obligation. (4) From simple privatization to privatization toward good performance.

As water has become a human right, the government, as well as public administration, has to reconsider the idea of privatizing the services closely (and directly) related to the government19. This is the first lesson learned. Public administration must redefine its basic mission rather than simply follow “fashionable” ideas. Ideas may be contemporary, but the basic mission should not be changed. A government has two basic missions: to develop excellent public policies and provide basic services. In regard to public policies, the excellence of a nation nowadays depends more and more on its ability to develop excellent public policies rather than on democracy. Good governance is more important than a good government. Basic public services must be redefined, since water is becoming a newly accepted human right20.

PPP privatization of government services may become beneficial depending on three key elements. First, often the government is unable, not unwilling, to actualize these benefits. Second, there must be an excellent policy structure as the platform for the privatization. Third, the process must take place within a good governance. There must not be any political pressure, either from local elites or international institutions, or both. Without one or two of the three key elements, the privatization process had better be called off.

This proposal is intended for both local and central governments, and global institutions setting global policies such as the World Bank, United Nations, and other global governance institutions. Water is for public consumption and not to be sold to the people. Before water becomes a matter of governance, it should become a government issue, because public policies, according to Thomas Dye (2011), are “what the government does, the reason they do it, and the difference it makes.” PPP policy will be a public policy as long as it creates a difference; a very good difference.

18 For Public to Public Partnership (PUPs), see PSIRU, 2009, Public-to-Public Partnership (PUPS) in Water, Transnational Institute.
19 The government has to able to think again, think across, and think ahead. See, Boon Siong Neo and Geraldine Chen (2009).
20 Australia and Japan define water as a government service; therefore, the institutions, investment, and management are controlled by the government. Britain, as the pioneer in public service privatization, now faces a new problem, that of increasing prices in its basic services, such as water and city transport.

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