

DOMESTIC PUBLIC FINANCE FOR WASH: WHAT, WHY, HOW?

This Finance Brief defines domestic public finance, and outlines why it is essential for providing universal water and sanitation services. This is the first publication produced by the Public Finance for WASH initiative, and can be considered a brief starting summary of what this initiative is about, and why it was set up.

WHAT EXACTLY IS DOMESTIC PUBLIC FINANCE?

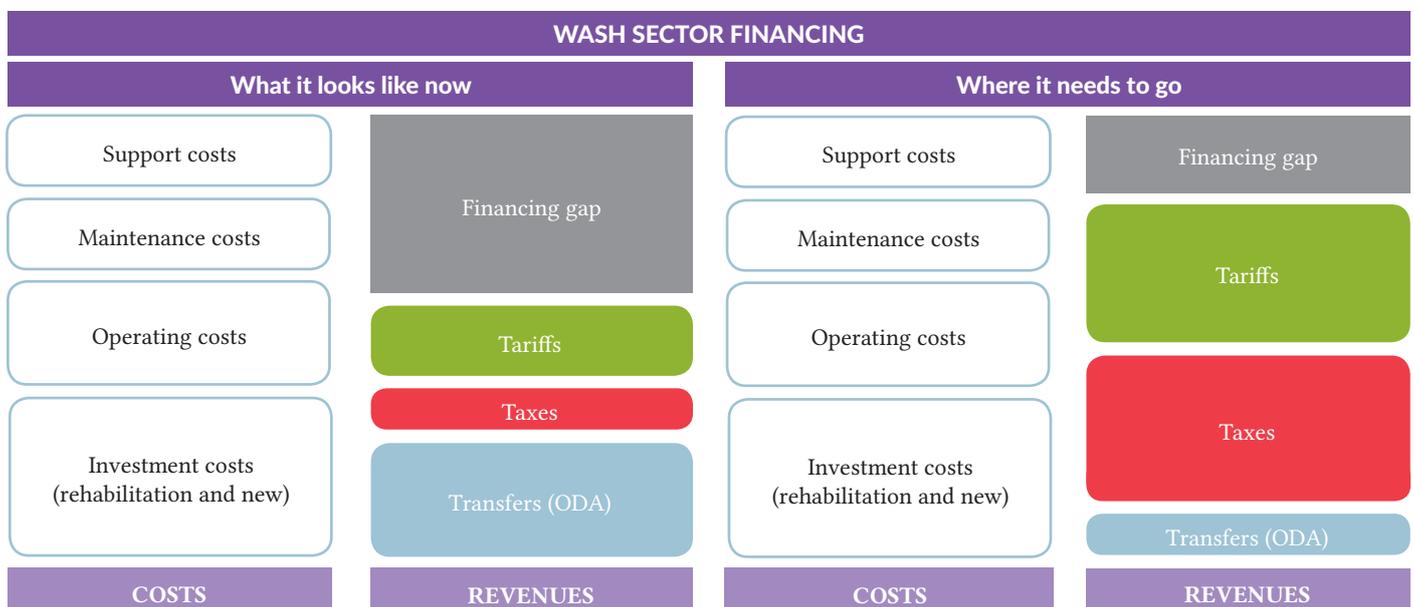
We define *domestic public finance* essentially as funds derived from domestic taxes, raised at the national or local level: for example, taxation revenues raised by the national government of Kenya or the municipal government of Nairobi.¹

Of course, domestic public finance is only part of the solution: service delivery in poor communities will invariably involve a mix of a) domestic public finance (derived from taxes and other sources of government revenue), b) user finance (derived from household payments for services received, i.e. from tariffs), and c) donor finance (i.e. development aid).² Likewise, domestic public finance forms part of a wider governance puzzle: improving WASH services requires not just more government investment, but also diverse other elements including (for example) clear institutional mandates.

Doesn't public finance inhibit markets? No! Public finance and market-based finance are two pieces of the same puzzle: both public finance and market-based solutions are essential for universal WASH. Spent correctly, public finance should create and stimulate markets.

WHY INVEST IN WATER AND SANITATION?

- The results of cost-benefit analysis indicate that water and sanitation improvements give a very high economic return on investment (ROI): for example, in East Asia the ROI is estimated at US \$8 for each \$1 invested in sanitation, and \$1.6 for each \$1 invested in water supply (global averages are \$5.5 and \$2 respectively).³
- The health benefits of investment in water and sanitation are enormous, particularly for children: water-related diseases cause 443 million missed school days each year, and poor health reduces children's cognitive potential.^{4,5} Investing in water and sanitation means investing in your country's future!



WHY IS DOMESTIC PUBLIC FINANCE NECESSARY FOR UNIVERSAL WASH COVERAGE?

There are powerful economic growth reasons for investing in water and sanitation: but why does this need public finance?

- Markets alone are not generally effective at providing “public goods” like large-scale water supply and sanitary environments: why should I invest, if I know that other people won’t? But if government obliges everyone to invest, by applying a tax, then most of us will be happy.⁶
- Markets likewise typically fail to reach the very poor: provision of basic services to the poorest inevitably requires public investment to support market-led solutions. Sure, poor-consumer markets can work well for things like mobile phones and biscuits; but generally not for WASH infrastructure!
- The historical evidence from rich countries indicates that domestic public finance has almost always played a critical role in creating and maintaining water and sanitation services, even in market-led economies like the US. User finance is certainly important, but the historical evidence consistently indicates a requirement for major injection of public funds derived from taxes: see our Finance Brief 2 Universal water and sanitation: how did the rich countries do it?
- The post-2015 development agenda places strong emphasis on domestic public finance.⁷ The post-2015 Sustainable Development Goals will likely include a specific target around increased domestic taxation. The SDGs are also likely to stress the importance of improvements that benefit the whole population.

SO HOW CAN PROGRESS BE ACHIEVED?

Low and low-middle-income countries throughout the world are making commitments to increased allocation of national budget to water and sanitation, under processes including the eThekweni process led by the African Ministers’ Council on Water (AMCOW), and the Sanitation and Water for All (SWA) initiative. However, formal commitments to increased budget are just a first step. How can governments ensure that those commitments become a reality, and that funds are allocated in genuinely cost-effective ways? How can effective

“If government obliges everyone to invest, by applying a tax, then most of us will be happy.”

mechanisms be developed for transferring funds from central government to local government? By what mechanisms can local government raise tax revenues locally? How can donor agencies and NGOs act in a way that supports development of effective public finance models? How can we accurately track how much public finance is being allocated to WASH?

These and many other questions (too complex to be answered in this very short note) will be explored by the Public Finance for WASH initiative over coming months and years. Our aim is to extensively document different solutions to the complex puzzle of public finance for WASH: watch this space, get in touch!

- 1 Funds derived from domestic taxation are the core focus of the Public Finance for WASH initiative; but governments may have other sources of revenue (including tariffs for services delivered, and income from sale or lease of land). And of course governments may take out loans or emit bonds; but this borrowing need to be repaid from taxes and/or some other revenue.
- 2 It is useful to distinguish between taxes and tariffs: a tariff is typically an optional payment, in direct relation to the costs of the service received; a tax is typically an obligatory payment, not necessarily in direct relation to the services received. But it’s not quite that simple. Consider for example a water tariff in which poor consumers pay less than the full cost of the services they receive, while wealthier consumers pay more: the cross-subsidy component in this tariff system is effectively a redistributive tax.
- 3 Hutton G (2012) Global costs and benefits of drinking-water supply and sanitation interventions to reach the MDG target and universal coverage.
- 4 <https://www.wsp.org/features/events/features/clean-water-and-sanitation-reduce-childhood-malnutrition-and-diarrhea>
- 5 Spears, D. and L. Sneha (2013). Effects of early-life exposure to sanitation on childhood cognitive skills : evidence from India’s total sanitation campaign. Policy Research working paper ; no. WPS 6659. Washington, DC: World Bank.
- 6 In more technical language, a clean environment is an economic good with low rivalry and low excludability; see for example Mason N et al. (2014) The technical is political: Understanding the political implications of sector characteristics for the delivery of sanitation services.
- 7 See e.g. Savoy CM & Perkins CM (2014) Taxes and Development: The Promise of Domestic Resource Mobilization.

PUBLIC FINANCE for WASH

The Public Finance for WASH initiative is grounded on two principles: i) that sustainable universal provision of high-quality water and sanitation services is fundamentally dependent on progressive domestic taxation systems, and that consequently ii) WASH-sector donors, donor-funded NGOs and in-country actors need to pay greater attention to ensuring that ODA is delivered in ways which support the development of effective and equitable domestic public finance systems.

Credits: This is a copyright-free document: you are free to use it as you see fit. Please cite as follows: “Norman G, Fonseca C & Trémolet S (2015) Domestic public finance for WASH: what, why, how? Finance Brief 1, Public Finance for WASH, www.publicfinanceforwash.org”.