

CONSTRAINTS TO PRIVATE SECTOR OPERATION

Maintenance of municipal infrastructure

This paper discusses the potential of the private sector to take medium- or long-term responsibility for the operation and/or maintenance of elements of infrastructure owned by municipalities.

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OVER AND ABOVE the service delivery benefits that could result, the paper also looks at the constraints to private sector involvement and what is needed to overcome them.

Given local government capacity constraints, it makes no sense for municipalities not to partner with the private sector where appropriate.

Why this discussion is needed

Prominent among the 'priority areas' causing problems is "insufficient municipal capacity due to lack of scarce skills". This is despite "national government [having] allocated hugely significant sums of money to building capacity over the years. In seeking to answer the question why outcomes have been so disappointing, it is clear government needs to begin to do things differently." (Ibid, pages 4 and 5.)

The chapter 'Service delivery and infrastructure' of the same report, while placing most of the emphasis on clearing backlogs by providing infrastructure to those that don't have,

also clearly puts across the need for vastly increased and more competent operation and/or maintenance of existing infrastructure. This comes across, too, in the Department of Cooperative Governance and Traditional Affairs' (COGTA) follow-up report on the "turn-around strategy". (COGTA 2010)

Disappointingly, however, neither report makes specific mention of the private sector as a potential resource. For instance, a scan of the 2010 report was unable to find the words 'private' or 'outsource'. Yet, the minister

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of Finance could say: "Why is it that a soft drink company can deliver soft drinks to its thousands of outlets on time and without any leakage, and yet our clinics are without drugs and medicines, and learner support materials arrive late or never arrive at schools?" (Ministry of Finance 2009)

In addition, the Department of Provincial and Local Government stated in 2006:

"Many municipalities are hampered by lack of flexibility in existing internal arrangements to deliver services and continued pressure on available human, financial and physical resources. Municipal service partnerships (MSPs) can allow a municipality to concentrate resources and management attention on its strategic core activities of planning and managing services within its municipality without having to be involved in the actual mechanics of service delivery." (DPLG 2006, page 4)

In our view, the private sector has the potential to help resolve many of the problems that municipalities periodically encounter with service delivery. In this paper, we emphasise, over other aspects of service delivery, the potential of the private sector to assist with operation and/or maintenance of infrastructure, and that this assistance could come with significant service delivery, societal and developmental benefits – furthermore, not necessarily at additional cost. There is no reason for municipalities to believe that in order to accept the assistance of the

private sector they have first to 'acknowledge' they have in some way 'failed'. Anywhere in the world there is a limit to resources and manpower. South Africa is no different.

The Institute for Local Government Management, in a notice of a 'breakfast session' in 2010, quoted Minister Trevor Manuel as having said: "Our priority is to meet the socioeconomic needs of all South Africans and, in particular, to alleviate poverty. We would be wrong to assume that government can meet this challenge alone."

The authors have no vested interest in the private sector; neither of us currently works, or has recently worked, for the private sector. Our interest lies only in finding ways to enhance service delivery. Personnel, equipment and systems are the means, not the end, and whether their operation and maintenance (note: their ownership is not part of this discussion) in any



"We would be wrong to assume that government can meet this challenge alone."
Minister Trevor Manuel

particular instance should be by the public or private sector, or a mixture of the two, should be a matter of what is in the best interest of service delivery.

How best to deliver services?

The service delivery functions assigned to municipalities in terms of the constitution are clear, as is responsibility for the ownership of the infrastructure. However, the constitution and other key legislation permit considerable flexibility when it comes to who operates and maintains that infrastructure. For example, water services authorities have responsibility for service delivery, but can use water services operators (as defined) – which can be public or private sector, or NGOs – as their agents.

In practice, however, the use by municipalities of the private sector to operate and/or maintain infrastructure is far more limited than it could be and less than it needs to be in view of both these driving factors:

- The chronic inability of many municipalities to operate and maintain their infrastructure themselves – which, while bound up with issues such as insufficient finance, has very often been shown to have a lot to do with lack of skills in the municipalities – as stated by COGTA (also the The South African

Institution Of Civil Engineering infrastructure report card, the Department of Water Affairs Water Services Infrastructure Asset Management strategy and many others).

- The private sector has many of the skills required, but these are seldom called upon by municipalities.

If the 'end' is service delivery that consistently meets performance specifications, and if the responsibility for the delivery and also the ownership of the infrastructure remain with the municipality, then the question of who operates and maintains that infrastructure should depend on the answers to pragmatic questions about how best to achieve that service delivery.

If a municipality is short of, for example, the technical skills to operate and maintain its entire infrastructure, would it not make sense for it to seek assistance from those who have the skills? While it is imperative that

strategy, planning, financial aspects (including tariff-setting) and other key issues remain with in-house staff, why not, where appropriate, outsource some of the day-to-day operations and/or maintenance?

There should be no in-principle objections, especially if the ownership of the physical infrastructure remains under municipal control and so do user charges, levels of service, prioritisation and other policy matters.

Outsourcing of operation and/or maintenance, when appropriate, can be viewed as an opportunity to improve infrastructure service operation and also as an opportunity to:

- retain income in the local economy
- develop human capital in the community (develop skills focused on the needs of the local infrastructure)
- facilitate the participation of communities in using the opportunities and stimulating the establishment of new businesses or the growth of existing ones.

In a nutshell: Whereas currently, the preferred institutional mode of delivery is municipal accountability for service delivery, municipal ownership of infrastructure and municipal operation and/or maintenance, a case can be made for trying out an alternative mode or at least for trying it out on a much greater scale than

it currently is. This could be municipal accountability for service delivery and municipal ownership of selected infrastructure, with private sector or NGO operation and/or maintenance.

The MSP guideline document succinctly sets out the 'rules' and also the 'purpose' of MSPs:

- While an MSP involves outsourcing municipal service delivery, a municipal council cannot outsource its accountability. Although MSPs change the means of delivering services, they do not change a municipality's accountability for ensuring that the services are delivered.
- Under an MSP, a municipality's focus shifts from managing the inputs of service provision to managing the outcomes. It becomes a contract manager rather than a resource manager. (DPLG 2006, page 3)

It might seem superfluous to make this point at all, but our experience has shown that first-time hearers of the suggestion that the private sector play a greater role in operation and/or maintenance of infrastructure sometimes automatically assume that indigent South Africans will now have to pay more for services. However, there is no reason to assume this.

If people currently receiving municipal services are indigent, and therefore benefit from the policy of free basic services, there is no reason why they would not continue to benefit irrespective of the institutional nature of the operator and maintainer of the infrastructure.

What the private sector could offer

The private sector is not homogenous and therefore the remarks in this section relate to what, at any given time and in any given circumstances, some private sector organisations could offer. Quite possibly the same organisations would not be able to offer these service inputs at other times and in other circumstances. It is even possible that other parts of the private sector could not offer these at any time whatsoever, or in any circumstances.

The CSIR recently cooperated with two organisations, one private sector and one public sector, both seeking to increase efficiency and reduce wastage. Both organisations own and operate large fleets of vehicles that are based at depots and travel to, and perform tasks at, many dispersed sites.

The CSIR found great differences in the will and the effort to ensure value for expenditure.

The drive to ensure value for expenditure was strong in the private sector case. For example:

- supply chain management was well planned and implemented

- vehicle usage was tightly controlled
- maintenance was carefully planned and speedily performed by qualified staff
- arrival at and departure from sites was tracked
- vehicle and equipment purchase, operation, maintenance and replacement were governed by life cycle cost considerations
- accountability was strong and the incentive structure reinforced this accountability
- any deviations from predetermined costs, standards and so on were reported to management, and ways were sought to improve future performance.

The drive to ensure value for expenditure was weak in the public sector case, for reasons both systemic and procedural. For example:

- supply chain management appeared to be weak or absent
- at any one time, a large proportion of vehicles were in maintenance workshops or otherwise out of action.
- measures to improve vehicle and equipment usage had been abandoned or had never been adopted
- tracking of vehicle movements was haphazard
- tracking of cost deviations and accountability for these was haphazard.

Why such a strong contrast with the private sector case?

Frankly, receiving value for expenditure did not seem to be a consideration. Assisted, no doubt, by the weak incentives to pursue value. But why is this the case? Why is there no apparent will to improve value for expenditure of the taxpayer's rand?

We cannot answer this question. But we can suggest that if some of the methods in common use in some private sector situations were applied, where appropriate, by their public sector counterparts, productivity would improve.

We hasten to add that we have chosen two particularly contrasting cases for the example above; we can point to many public sector organisations where value for taxpayers' expenditure is a strong driver and it shows in the results that they achieve.

In our view, the private sector could, in appropriate circumstances, offer public sector entities four types of benefits:

- Flexibility: the private sector can be contracted to provide a specific service over a specific period of time, after which the costs associated with the contract are no longer borne by the public sector entity. Resources no longer needed are not an ongoing expense to the public sector entity.
- Sharing of contractual risk.

- Because the private partner would only be paid for measurable quantities and output, the public sector entity can be more certain that spending will result in predefined deliverables.
- Skills: including management skills. 'Appropriate circumstances' would have to include competent contract documents, competent public sector client staff, competent private sector staff, adequate budgets and so on – none of which can be taken for granted.

Sharing of risk

If a contract was appropriately structured, and the relationship between the municipality and

can be priced and measured

- cost control: thanks to the above, the financial consequences of undertaking more or less work, or different work, can be understood both before the decision is made whether or not to proceed with the work, and after, when the entity is called to account for the expenditure.

If a municipality needed a specialist skill, but did not need it all the time and indeed could not afford to retain it, it would make sense to hire this skill only when needed. A private sector contractor that is hired to undertake a specific task has to manage the entirety of the resources that it needs; failure to do so is its responsibility, not that of the municipality.



Hiring a contractor to operate and maintain, say, a water services system places the onus on that contractor to assemble and manage all the needed resources

the contractor is one of equals, risks can be equitably shared. That is, the consequences of natural events, financial events, construction events, labour events and so on can be shared in a previously agreed manner and not entirely borne by the public sector, as would inevitably be the case were the public sector entity undertaking the task itself.

Regarding measurable quantities and output, and payment for work done (presuming appropriately structured contracts and relationships), the following can be ensured:

- transparency: work is done for an agreed price, is measured and the agreed payment flows
- control of variations: if variations on the original quantities and output are required, these too

Hiring a contractor to operate and maintain, say, a water services system places the onus on that contractor to assemble and manage all the needed resources. Ordering materials on time and employing qualified staff are part of the job and the consequences of not doing so are at his cost. When the contractor makes a mistake and has to repeat work, the municipality does not pay more, whereas if the mistake was the municipality's, it would have to bear the extra cost. The municipality buys the management – the teamwork – and the burden of resourcing and managing the team is transferred from the municipality to the contractor.

We concede that these are generic statements. The advantages and disadvantages

enumerated above would not necessarily, in respect of other municipal service delivery activities, be as apparent.

It bears repeating that outsourcing requires a knowledgeable client. A municipality's competence to monitor performance and enforce contract compliance is the key to it effectively using the private sector. But if a municipality is short on management resources, it would, in appropriate circumstances, be putting those resources it does have to more efficient use if it managed the work it outsourced rather than trying to cope with the operational issues itself.

Constraints to outsourcing

There are four issues that, in our experience, are most frequently cited as constraints to involving the private sector in operations and maintenance of municipal infrastructure. These are:

- the financial status of some municipalities
- for sometimes related reasons, municipalities

not honouring all of their contracted obligations

- union resistance
- procurement processes – in particular, application of the Section 78 process of the Municipal Systems Act (South Africa 2000).



Before it can consider outsourcing, a municipality must undertake the Section 78 process

On the first two of these points: The financial affairs of many municipalities are not in order. Many are not able to recover all of the revenues due to them. Financial constraints specific to outsourcing of operation and/or maintenance

include widespread under-provision of finance for operation and particularly maintenance. This situation may be exacerbated by a tendency, for a variety of reasons, to transfer funds out of maintenance budgets during the course

of the financial year. Inability to always follow acceptable accounting and payment procedures, including inability to process invoices and pay them on time, is sometimes in evidence.

None of this bodes well for private sector involvement in the provision of services. Furthermore, inability to pay invoices on time presents considerable problems for outsourcing even to larger contractors. It would very likely be fatal to small enterprises,

which have few reserves and might be dependent on only a few clients or even on only one client.

Regarding the point, there are indications that some unions will resist any outsourcing of

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municipal service provision for fear that it could lead to retrenchment of their members.

On procurement

The Department of Water Affairs, COGTA or National Treasury policy, legislation and regulations are permissive of outsourcing of infrastructure services operation and management. This outsourcing can be a public-public partnership, public-private partnership or a partnership with a non-governmental organisation (NGO) or community-based organisation. Legislation relating to outsourcing and procurement by municipalities mainly relates to procurement of private sector service providers.

National Treasury and COGTA legislation and regulations are aimed at transparent and equitable procurement, and include anti-corruption measures, such as sequential approval responsibility for evaluation and adjudication committees. There are also measures to depoliticise procurement, through barring councillors from membership of certain committees, for example. We strongly support this legislation.

Before it can consider outsourcing, a municipality must undertake the Section 78 process. However, if it is not considering outsourcing, it is not required to demonstrate that it can provide the service in-house better than any outsourcing alternative could. Thus, in practice, too few municipalities go to the trouble of seriously considering alternatives to in-house operation and/or maintenance of infrastructure services. We feel that all municipalities should be encouraged to undertake Section 78 investigations in order to determine to what extent they are best able to carry out their responsibilities for operation and/or maintenance in-house – and thereafter to determine to what extent they should outsource.

By denying themselves the opportunity to explore alternatives through an objective Section 78 process, these municipalities may have no reliable financial or information-supported rationale for the decisions they need to take in the interests of improving services to their customers. At very least, municipalities should be required to assess the full costs of

the in-house option, so that these costs can be better understood.

It is understood that there are significant capacity constraints in some municipalities that could prevent them doing this kind of analysis at all, let alone doing it properly. On the other hand, if a municipality cannot do the analysis, it is not likely to be able to perform the service properly in-house. That should be good enough reason to investigate alternatives in these instances.

Overcoming constraints

Municipalities need to be supported in their efforts to procure and contract with private sector providers. Two broad categories of measures to assist in overcoming the constraints noted above can be identified:

- support in the form of people or units
- support in the form of procedures, protocols, documentation and the like. **SS**

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