

Options for the extension of the ACP-EU Water Facility under EDF 10

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Executive Summary

The ACP-EU Water Facility (WF) started operations in 2004 with funds of EUR 500 million, awarded to applicants following two Calls for Proposals. The First Call has been largely allocated and disbursements started in April 2006, while the results of the Second Call are imminent.

The WF's aim is to stimulate increases in finance for water and sanitation (W&S) and to support the Millennium Development Goals in this sector. Grants of up to 75% of the cost are available for projects that improve the access of the unserved poor to W&S, including reforms to governance, steps towards integrated water resources management (IWRM) and partnerships with civil society organisations. The WF is a challenge fund¹, in which applicants are chosen on the merit of their proposals in a competitive manner. Innovation and financial additionality are important criteria.

There is strong support in some quarters for a continuation of the WF into EDF10. Its advocates point to its market niche - its ability to operate at sub-sovereign levels, to work with a wide range of partners, and to finance water projects in ACP countries that do not give priority to W&S. It fills an unsatisfied demand – which was proved by the large excess of applications over funds available. It is strongly supported by many NGOs active in this sector for its empowerment and capacity building at the grass-roots level.

At the same time, the WF has aroused concerns. Some have argued that the WF has distracted donors and recipients from the urgent need to increase conventional sources of funding for W&S. There is a desire in some quarters for using the WF in a more direct and pro-active way to develop national water strategies and policies, and avoid the risk of undermining national policies and structures. There is, it is argued, not enough sense of ownership of the WF by African Governments, and decisions over its allocations should be further decentralised. Feedback from NGOs has suggested a number of ways in which the working of the WF causes problems for potential applicants.

In some ways, too, the initial expectations of the WF have been disappointed. There is little evidence of innovation or risk-taking and, while the WF has complemented existing sources of finance it has attracted little new money. Important local players have not come forward, such as municipalities, banks, and local water operators. International agencies and external NGOs are over-represented in allocations.

This report sets out options for the WF in the form of a Decision Tree. The first decision is whether to continue funding the WF from EDF10. Although there are arguments against, we believe they are outweighed by the case in favour of continuation. The second decision is whether to allow Member States to co-fund the WF on a voluntary basis along with the EDF. On balance, we think this should be supported. Thirdly, and assuming the WF continues to be funded by EDF10, decisions have to be taken about whether its aims, policies and modalities need to be reexamined. We believe that they do, and that an independent Mid-Term Review of the WF during 2007 would be an excellent opportunity. The report ends with a list of proposals for the independent review to consider.

¹ Though a small share of the funds is made available through direct negotiation, e.g. to river basin organisations.

Glossary of Acronyms

ACP	Africa, Caribbean & Pacific
AMCOW	African Ministerial Council for Water
DFID	UK Department for International Development
EDF	European Development Fund
EUWI	EU Water Initiative
FWG	Finance Working Group (of the EU Water Initiative)
HDR	Human Development Report (of the United Nations Development Programme)
IFI	international financing institution
IWRM	Integrated Water Resource Management
MDG	Millennium Development Goal
MS	Member State (of the European Union)
NEPAD	New Partnership for Africa's Development
NGO	non-Governmental Organisation
ODA	Official Development Assistance
SSA	sub-Saharan Africa
WF	ACP-EU Water Facility
W&S	water & sanitation

1. The Political Background

In July 2006 a group of eight NGOs wrote to Commissioner Michel requesting an extension of the ACP-EU Water Facility (WF) under the 10th European Development Fund (EDF). Following comments on this proposal by DG/Development, the matter was briefly raised at a meeting of the EUWI Finance Working Group (FWG) in Stockholm in August.

In October 2006 DFID called for the EU to provide more resources for water and sanitation (W&S) “through a reformed ACP-EU Water Facility, under EDF 10, better linked to the EU Water Initiative so that it is much more strongly integrated with national and local planning”. Informal consultations by the FWG revealed backing for this proposition among other EU MSs.

Aid donors are on the defensive, faced with the decline in ODA for W&S since 2002, contravening the commitments given at WSSD (2002) and by the G8 Water Action Plan (2003). This is highlighted most recently in the UNDP Human Development Report 2006. Against this background the WF has the potential to bypass many of the constraints and bottlenecks associated with central government, and target resources to decentralised local and municipal service providers.

Despite this, it has attracted criticisms of various kinds, e.g. lack of close involvement by development partners such as the African Ministerial Council on Water, and teething problems in reconciling its procedures and policies with the needs of local parties.

There are different views on whether ODA should be earmarked for specific sectors such as water, and there are competing claims for the intra-ACP funds within EDF 10. Despite this, there is a strong case to reinforce support to W&S in EDF10 through a continuation of the Water Facility in some form. There is need for a thorough, critical and independent review of what the Water Facility has achieved, and how it might be reformed and improved, to identify how it should be re-designed and implemented under EDF10. It is not a foregone conclusion that the Water Facility will be extended. The EUWI must raise the matter, argue the case for more resources for W&S, and provoke the debate.

In this context FWG has prepared this paper for the EUWI Steering Group containing options for a possible extension of the Water Facility under EDF 10. A preparatory meeting was held in London in December 2006 with several NGOs concerned, followed by meetings in Brussels with officials of DG/Development and the Water Facility Unit. The purpose of the paper is to generate debate among the EU MSs and stakeholders active in the EUWI.

2. Essential features of the Water Facility

The WF was launched in 2004 in order to catalyse more funds for W&S in ACP countries. An amount of €250 million for the WF was approved by the EU Council in 2004, and a further €250 million in 2005, both from the “reserve billion” within EDF 9.

The objective of the WF is to help address the financing gap in the sustainable delivery of water and sanitation services, and promote water governance and IWRM practices in ACP countries. Its higher aim is to contribute to poverty reduction and sustainable development through achievement of the W&S Millennium Development Goals. The EU Council Conclusions (March 2004) which adopted the Water Facility directs that :

“The funds of the Water Facility will be primarily used:

- in innovative ways, notably addressing issues raised by the 2003 report of the World Panel on Financing Water infrastructure (“Financing water for all”), and by the report of the Finance Working Group of the EU Water Initiative;
- in co-financing arrangements, to provide grant-funded elements of projects to enhance the access of the poor to water and sanitation services, according to Article 65 of the Cotonou Agreement and relevant articles of the Financial Regulation for the 9th EDF; in principle, the Facility should not provide the majority share of funds for individual investment and private sector projects;
- to finance capacity and institution building, integrated water resources management activities, and contributions to existing initiatives within a concrete financial framework;
- considering activities described in the documents from the EUWI Working Groups on Water Supply and Sanitation and on Integrated Water Resource Management;
- as a catalyst or enabler, the Facility will complement and add value to other work to catalyse action, rather than operate as a standalone financing instrument”.

The WF is a so-called challenge fund: most of its resources are made available through a process of Calls for Proposals. The first Call for Proposals, closed at the end of January 2005, resulted in the receipt of about 800 proposals requesting a total funding of €2,75 billion for projects of a total value of €5 billion. The funds made available for the first Call for Proposals were limited to €180 and this was supplemented with €50m from the second tranche of the facility, giving a total of €230 million. 97 projects were selected for support.

The second Call was launched in March 2006 and resulted in 460 accepted applications requesting a total EC contribution of about €1.1 billion, more than five times available funds of €180m. The results of the second Call are still being analysed and will be made public in February 2007. But already they confirm the high demand noted in the first Call.

EDF 10 provides a total of €23.6 billion for the period 2008 to 2013, as against €13.5 billion under EDF 9. The bulk of these funds will go towards funding the EC cooperation programmes in the 76 partner countries within the ACP. In EDF 9, 16 countries had W&S as one of their priority sectors, with allocations of €500 million; in EDF 10 current indications are that although more countries are likely to receive support for W&S, the overall allocation is likely to be less. This implies a greater priority for water in the new EDF but paradoxically a lower level of funding commitments. One explanation is that the share of budget support has risen from 30 % in EDF 9 to a target of about 50 % of the much bigger EDF 10. .

The intra-ACP component of EDF10, out of which any extension of the Water Facility would be financed, is €2,7 billion, and a decision by the Commission regarding the allocation of these funds has not yet been taken. It is expected that the intra-ACP funds will be used, amongst other things, for the EU-Africa Infrastructure Partnership and support to the African Union in a number of areas. The unique circumstances under which the Water Facility could be established under EDF9, from the conditional €1 billion, do not exist under EDF10 and it cannot be taken for granted that an allocation of the same size, €500m, could be made available under EDF10.

New Regulations under EDF10 are likely to allow MS to make additional contributions to the EDF. If implemented, MSs could earmark any additional funding they might consider to supplement an allocation from EDF10 to a WF.

3. Assessment of the Water Facility

WF's niche & added-value

The WF occupies a market niche due to its ability to:

- operate at sub-sovereign levels (unlike most other EDF products, where the EU counterparty is central government). Budgetary aid, which is expected to rise to 50% of all EDF country programmes, also works through the central budget: it is difficult to channel these resources to W&S where local governments do not give this sector the same priority as external donors.
- work with a wide range of parties involved in service delivery (e.g. NGOs, river basin agencies, local private firms).
- function in ACP countries that do not prioritise water in their EDF country programmes and would not otherwise receive EDF country allocations for this. From a water sector standpoint this confers *additionality*.^{2 3}

The WF's offer of funds for W&S at the sub-sovereign level and its support of decentralised partners responds to two of the key themes of the Camdessus Panel. This is a source of added value (Box 1).

Box 1: Added value of the Facility: an NGO viewpoint

- It recognises the role of local authorities (sub-sovereign authorities) and their complementary role to that of central Government in specifying and implementing development strategies, as well as the relevance of the local level in meeting the challenge of achieving access to water and sanitation for all
- It is one of the few financial mechanisms from international donors which supports directly projects and programmes at the local and sub-sovereign level (including water boards, public utilities, municipal agencies, local/ domestic private sector, local including community partnerships, NGOs, etc. (a bridge between local demand and donor supply, supplementing necessary resources at local level).
- The principle of call for proposals encourages local actors to improve their capacities to formulate and manage projects in partnership with other stakeholders
- By encouraging the creation of partnerships between local stakeholders, it opens the possibility for scaling up, moving from project approaches to programme approaches, and building local or regional policies,
- It ensures consistency between accepted proposals and national policy and strategy by considering this point as one of the key selection criteria
- It transfers skills for negotiating with donors to local project management level.

Source: paper by PsEau et. al.

² The current WF originated from a EUR 1 bn reserve fund being held back by the Commission pending evidence of disbursement of EDF. In this sense, the WF has provided "additional" resources for W&S.

³ From a management standpoint this introduces a new set of difficulties, since the Commission has delegations in all 76 ACP Countries, but supports water and sanitation through its national programmes in less than a quarter of these. Where the Commission Delegation is not active in the water sector, it is unlikely that the Delegation will have staff with the necessary technical expertise and time available to manage the extra work

Performance of the WF

As noted above, the results of the First Call for Proposals, and preliminary indications from the Second, indicate a high and unsatisfied level of demand for this kind of finance. The majority of the bids in each Call satisfied the WF criteria. The novelty of the WF is evident from Box 1. It should be added that the WF also engages the EDF with a new spectrum of development organisations, e.g. river basin and regional organisations, and cities involved in "twinning".

On the other hand, some critical observations have been made:

- there is not enough evidence in bids received of innovation and risk taking in service delivery, technological options, or funding methods (recall that innovation receives pride of place in its original aims)
- although the Facility has been able to complement existing sources of finance it has had little success in leveraging "new" sources (though what is "new" can be debated – all applicants have to contribute a share of the project costs)
- there has been a disappointing level of interest from the local private sector, e.g. water operators, banks, microcredit agencies.
- UN agencies and international & overseas NGOs are over-represented as co-funders and beneficiaries
- fewer bids than expected have been received from municipalities

The WF Unit estimates that, as a result of allocations under the First Call for Proposals, by 2010 around 10 million people will benefit from improved access to drinking water and 5 million to sanitation.

A consultants' report (COWI) in mid-2005 explored reasons for the lack of "innovative" financial solutions in proposals made to the WF and implied that the original aims of the WF in this area may have been overstated.

The WF Unit reports an improvement in the quality of proposals received in the 2nd Call, compared with the 1st., possibly evidence of a "learning curve" under way.

An independent evaluation of the WF is due to be carried out in 2007.

Some concerns expressed

This section reviews some of the main concerns expressed by NGOs and others about the WF and the way it has worked so far:

The WF should provide greater support for national policies and strategies and sector investment plans. It should avoid anything that undermines existing processes.

The award of WF grants appears to bear little relation to countries' W&S strategies and policies. They do not result from a systematic analysis of strategic needs nor the elimination of specific bottlenecks in each country. Indeed, there is a risk of local parties "breaking rank" and by-passing (or even undermining) systems and procedures in order to get funding. There are many examples of apparently successful local projects which by-pass national budgets and administrative procedures. On the other hand, many proposals are supported by governments

and help to provide funds and capacity building to supplement the government's resources. The WF Unit insists on adherence to national policy as one of its selection criteria.

This raises a fundamental question whether a challenge fund like the WF can support priority national actions, while retaining its competitive aspect and backing innovation? Is it feasible to require coherent national water strategies and policies for each of the countries from which applications originate, and to require proposals to conform to these? How can this top-down approach fit with bottom-up initiatives and demand-responsiveness, which are often the originators of reform?

It is worth remembering that Component A of the WF is aimed at "Improving Water Management & Governance", which would include policymaking and strategy. Formulating a national strategy and policy has to accommodate "bottom-up" local initiatives into "top down" decision-making, and often successful programmes start locally outside official national plans. National W&S programmes are likely to evolve as a synthesis of central and local forces, and meanwhile the latter will be stifled without funding.

The extent of ACP and AMCOW ownership and involvement in the WF.

AMCOW has argued that the WF does not respond to African needs or wishes. It should be recalled that the WF differs from the African Water Facility, which is a specific creation of AMCOW and subject to its ultimate control, whereas the WF is jointly owned by the ACP (represented by the ACP Ambassadors' group in Brussels) and the EU. The ACP Secretariat is the official contact point for the WF with the ACP parties and governments. AMCOW has some influence on ACP Ambassadors, and *vice versa*. Formally, the ACP Council backs the WF (see below). In reality, many ACP governments do not give priority to water in their public spending decisions. The WF cannot compensate, except marginally, for the lack of priority given to water in most EDF country programmes, a factor which needs to be addressed head-on (and which the EUWI tries to do).

One of the seven members of the WF's Evaluation Committee is an ACP nominee (practically the first time the Commission has had external formal evaluators in a Call for Proposals). The Commission's official dialogue partner for the EDF is the ACP and other regional organisations such as AMCOW would need to focus on the ACP Ambassadors in making their representations about the WF. A stronger and clearer relationship between the WF & the AfWF is desirable (it should be recalled that the WF already provides a EURO 20 million grant to the AfWF). However, so long as the challenge fund concept is retained, there are limits to the possible influence of AMCOW or any other external political body. It should also be remembered that AMCOW does not represent Caribbean and Pacific interests.

The ACP Council is on record as supporting a continuation of the WF. The *communiqué* of its Khartoum Meeting of 8 December 2006 contained the following text:

"...Reiterate our resolve to increased access to safe, affordable, and sustainable water supply, smallscale irrigation, especially through the maximum utilization of traditional irrigation systems and local technologies, as well as increased and improved affordable sanitation services. In this regard, we reaffirm our support to the activities of the ACP-EU Water Facility and call for the funding of the Facility to be extended to the 10th EDF".

The allocation of funds between countries does not target the neediest countries and regions

Within a demand-responsive challenge fund there could be a tension between need and poverty – on the one hand - and absorptive capacity, preparedness and bid flow – on the other.

There are several ways of approaching this problem. It could be argued that the resources of the WF are small in relation to the financial needs of the MDGs, which are better addressed by flows from bilateral donors and IFIs. On this view, the role of the WF is to foster innovative solutions, and to pilot schemes capable of wider application both inside and outside their countries of origin. Unserved populations targeted by the MDGs exist within ACP countries at all stages of development, not just those with the lowest average GDP per head. It is a counsel of perfection to make fine distinctions between countries, many of which are poor in absolute terms. EDF funds provided under the Cotonou Agreement are available to ACP countries at various levels of income per head. There is also the practical point that a number of the most needy ACP countries are “fragile states” undergoing civil wars. These are difficult environments for the implementation of development projects.

Given a desire in some quarters for allocations from the WF to be more closely aligned with MDG⁴ needs, the options are:

- i) pre-set country allocations in favour of countries lagging on their MDG targets. . This would probably be resisted by the ACP and would complicate management by the WF Unit – even leading to underspending from individual country allocations.
- ii) positive discrimination exercised by the WF Unit in evaluating bids to give a greater weight to MDG fulfilment (The criteria would need to be clearly formulated, otherwise this could obfuscate bid evaluation and selection).
- iii) pro-active attempts to stimulate awareness and demand in target countries, with help in preparation of bids. This is probably the most realistic and feasible option, and some bilateral agencies have taken such initiatives during the 2nd cCall for Proposals.

Most successful bids have been sponsored by international agencies & international NGOs

The majority of Awarded Proposals signed from the 1st Call for proposals have been sponsored by UN specialised agencies⁵ and international voluntary agencies & NGOs⁶. Do these bodies “crowd out” worthwhile local bids, or, on the contrary, do they facilitate and strengthen bids from their local partners? Is it fair that international agencies and other bodies already receiving grants from their own governments get “two bites of the cherry” by receiving awards from the WF? It is not clear what the philosophy of the WF is on this matter. Possibly a pragmatic approach should be adopted, favouring proposals which strengthen local institutions and promote programmes with a strong local ownership, even if some of these are sponsored by international bodies. This issue needs to be further aired.

Other criticisms have been of the *procedures and management* of the WF:

⁴ Pro-poor is not the same as pro-MDG. Income levels do not fully explain a country’s progress towards its MDG targets. For the WF, the MDG is the more appropriate criterion.

⁵ 12 of those so far signed in the First Call.

⁶ 46 of those so far signed in the 1st Call

- *Management of the WF should be more decentralised, with a greater voice to the final users.*

Critics have dwelt on the distance between Brussels, where decisions on selection are taken, and the ACP countries where funds are to be applied. There has been a call for the involvement of regional intermediaries to manage the process⁷. It is alleged that assessors need to be better acquainted with local circumstances and the national W&S situation.

The importance of adequate national and local knowledge of W&S needs is obvious, and the WF should, and no doubt does, avail itself of all feasible sources of advice and information. However, while decisions on the allocation of funds need to be fully informed of the local context of bids, they must also be consistent, accountable and independent of local pressures. This may be easier for a central decision-making body. There are avenues open for Delegations to supplement their expertise for making local assessments of proposals.

At present, Delegations are responsible for negotiating contracts and managing projects in their countries. Additional support should be available to them where the WF entails unpredictable and intermittent extra work. The case for this is even stronger where the Delegation does not have water as a priority sector.

There are unnecessary delays between submission of bids, decisions, & disbursement.

The First Call for Proposals was launched in November 2004 and project selection was made in January 2006. By October 2006, some 76 projects had been signed for €146 million, with the remaining 21 for €82 million close to signature. The Second Call was launched at the end of March 2006, with a deadline at the end of June, a target for completion of evaluations by November, and the expectation of decisions on allocations by February 2007. Projects will need to be signed by the end of 2007.

If this timetable is met, the Second Call will turn out to be speedier than the First, largely because of the adoption of a single-stage submission rather than a two-stage process⁸. There are several options for further reducing the cycle. Firstly, the Unit could revisit proposals from the First and Second Calls that were of acceptable standard but which were not selected because of budget constraints. Secondly, Calls for Proposals could be made smaller and more frequent, to give applicants more time to prepare good bids and avoid rushed bids submitted so as not to “miss the boat”⁹. This would also relieve some administrative pressure on the WF Unit. Thirdly, a closer targeting of aims and beneficiaries would reduce the universe of applications to a more manageable number.

Time spent on unsuccessful bids is wasted and the WF has distracted officials from more fruitful work (Box 2)

Box 2. The Water Facility as a wasteful distraction

⁷ in the paper by pS-Eau et. al.

⁸ for the sake of balance it should be pointed out that some smaller NGOs preferred the procedure in the First Call, of Preliminary proposals, followed by detailed bids, even though it was slower than that in the Second, where Concept Notes were required.

⁹ because there would be further opportunities to submit bids

“The EUWF has actually had a negative effect by distracting hard-pressed officials. They have focused on submitting proposals – the vast majority of which will be unsuccessful since the EUWF was 15 times over-subscribed – rather than, for example, on lobbying their own governments to prioritise the water and sanitation sector more in the allocation of debt relief monies or aid increases. This is exactly what has happened in the EUWI Ghana dialogue.”

Source: An empty glass: the EU Water Initiative's contribution to the water and sanitation Millennium targets. A Discussion Paper of WaterAid and TearFund, December 2005

In a challenge fund where money is awarded competitively there will always be disappointed applicants. The same is also true of a “first come first served” process such as that used by the AfWF, wherever the budget is oversubscribed. An over-subscribed fund is a sign of demand that is unsatisfied by other means. It should be recalled that all funding proposals, from whatever source, need time to prepare, and may be unfruitful. A challenge fund with a Call for Proposals structure will always introduce unpredictability into future aid flows. Because of its scale and concept the WF is complementary to conventional aid programmes, and is not a major source of aid for W&S in its own right.

The “opportunity cost” of time spent applying to the WF is debateable. It is doubtful if the WF can be blamed for officials’ lack of success in convincing Ministers of the case for funding W&S. There is a contrary view (Box 1) that the very process of forming partnerships and drawing up proposals is itself a useful form of capacity building.

Could the WF be better publicised amongst potential applicants?

Specifically, the role of Delegations in spreading information about Calls for Proposals is deemed ineffective. Whether or not this is fair, there is clearly scope for more pro-active efforts to raise awareness of the WF and stimulate demand amongst target agencies that have shown little interest so far (e.g. municipalities, local water operators, micro-credit agencies). Again, the problem is greatest with those Delegations that do not work in the water sector. It would appear that this problem could only be addressed through awareness raising in combination with provision of local consultancies whenever suitable.

Should applicants get help to prepare sound bids?

It is alleged that potential applicants lack experience in assembling partnerships and submitting proposals according to the format and timetable required by the WF. This is likely to be a greater problem for agencies at sub-sovereign and local layers of society, which have difficulty investing the resources necessary to produce a good proposal.

During the Second Call several bilateral donors (UK, Netherlands, France, Austria) provided independent help to applicants in assembling their bids. Building on this development, the WF could be used to assist the preparation of proposals, either by using part of the budget for co-funding the various bilateral initiatives, or assist on a project-by-project basis.

The second option would require the WF Unit to choose which applicants to subsidize (without having information about them or their proposal). It could prejudice the decision of the Selection Panel in specific cases, and a sizeable part of the WF might be taken up in the preparation of bids which turned out to be nugatory. Another approach would be to stagger the Calls for Proposals to give applicants more time. It should also be noted that the WF has a Help Line which has been quite well used.

There is presently a large excess, rather than a shortage, of demand for the WF. Any specific support for preparation of proposals should be closely targeted to those countries or socio-economic groups whose interest is considered worth encouraging, though as noted above this may be problematic.

4. The need for finance for water supply and sanitation

The most recent estimate of the financial gap facing SSA in achieving the water and sanitation MDGs is at least US\$2 billion annually (Table 1). A major part of this deficit is at the sub-sovereign layers of administration on which implementation of the MDGs will rely – state governments, municipalities and local communities that are badly catered for under conventional financing arrangements. The *desideratum* for W&S financing is long term, local-currency finance on affordable terms accessible to sub-sovereign and decentralised entities.

Table 1. Annual investment needs & financing gap for sub-Saharan Africa

	% of GDP	Bn US\$ p.a.
1. Cost of reaching MDG target 10 in SSA, during next decade	2.7	7.0
2. Current public spending on W&S in SSA	0.3	0.8
3. Greater cost recovery & mobilisation of finance from communities	1.0	2.5
4. increase in items 2 + 3 on optimistic assumptions	1.6	4.1
5. current external aid	0.3	0.8
6. gap between 4+5 and 1	0.8	2.0+

source: UNDP Human Development Report 2006

The arithmetic in Table 1 clearly indicates that more external water finance is needed in SSA and ACP countries, whether it comes from the WF, conventional bilateral country donor programmes, or other sources. In the timescale of the MDGs, the original mission of the WF to stimulate unconventional funding sources, to leverage additional funds, and to help local initiatives get to scale, is more than ever necessary, and needs to be reinforced.

5. Options and Proposals for the Water Facility

Decisions have to be taken in the following sequence:

- Should the WF continue, as part of the EDF10 package?
- If so, should it be wholly funded from EDF10 resources, or should it be co-financed by EDF and voluntary contributions from the Member States (MS)?
- If it continues, how should it operate, and what changes need to be made?

5.1. The case for a continuation of the Water Facility in EDF10

The following are key considerations in the decision to extend the WF (Box 3):

- Does the WF represent real value-added in financing W&S, or does it duplicate or detract from other, more conventional, sources of finance?

- Has the existence of the WF weakened the efforts of bilateral and multilateral donors to increase their commitments to W&S? Has it reduced the willingness of ACP countries, Delegations and EDF country programmers to give priority to W&S? Has the WF been at the expense of the EU Water Initiative?
- Is there a case for a fund earmarked solely for W&S at a time when other sectors highlighted by the MDGs are also clamouring for funds? (It is relevant to note that W&S is the theme of the 2006 Human Development Report, which makes a powerful case for adequate investment in this sector; and that 2008 is designated as the International Year for Sanitation)
- Is it too early to commit to a continuation, before there is any experience from the current one? (Although disbursement have started from the First Call for Proposals, allocations from the Second will not be known before Feb 2007).
- If it were to continue, the WF should demonstrate complementarity and additionality, compared with other existing funding sources. Can this be done?
- Would NGOs be able to fund their ACP activities from other sources, e.g. the Commission's annual call for proposals from civil society organisations, and other existing donor sources ?

Box 3. The decision process to extend the Water Facility

The steps that need to be taken to extend the WF under EDF 10 may be briefly summarized as follows:

- A request to the Commission will need to be raised by the ACP Committee of Ambassadors in Brussels.
- If that request is received, it will need to be presented to and confirmed by the ACP-EU Joint Council which meets twice per year.
- Once so confirmed, the Commission will prepare a financing proposal for submission to the EDF Committee.
- The EDF Committee, consisting of the EU MS, will consider the financing proposal and present an opinion, following which the Commission will take a decision.

The process will thus be triggered by the ACP Committee of Ambassadors. There are several ways to raise the matter with this group. One is for interested EU MSs to approach the Commission which is in current contact with the ACP Committee of Ambassadors through its Secretariat in Brussels. Another may be for those same EU MSs to lobby the Chair of the Committee and key members through their own ambassadors in Brussels. A third will be for African (and other ACP) governments to instruct their Brussels-based ambassadors.

African water ministers should exercise their influence through the third route above. As mentioned, they have complained that they have had no influence over the design and implementation of the Water Facility, given its nature as a challenge fund. It has been carefully explained by the Commission to AMCOW representatives, including the AMCOW Chair, how the Facility functions and through which channels they can transmit their views and the Commission arranged a meeting between the AMCOW Chair and the ACP. But the link between AMCOW and the ACP Committee of Ambassadors is tenuous, since it has appeared in practice to be difficult for African sector ministers to instruct to their own Brussels-based ambassadors. Nevertheless, the EU should encourage AMCOW to pursue this route and convey a clear message on the extension, or not, of the WF. It is likely that such a message would weigh heavily in the final deliberations on any such extension.

5.2. *WF wholly funded from EDF10, or co-financed with MSs?*

The following are factors to consider:

- There is no certainty that, if a decision is made to continue with a (reformed) Water Facility, EDF10 funding would be as large as the €500m made available under EDF9.
- Additional voluntary MS funding of EDF 10 may be allowed and co-financing is encouraged under EDF 10. However, complications may arise if the MSs attach conditions to their financing (e.g. to focus it on particular countries or sub-sectors)
- The likely financing gap for SSA (and even more so for the whole ACP) to meet its MDG targets for W&S (about US\$2 billion annually) is a great deal more than the amount that can be provided by a Water Facility at its current scale plus the funds provided through National Indicative programmes for this sector.
- Some EU donor agencies may prefer to associate their aid for W&S with the WF, rather than ‘going it alone’, one motive being to economise personnel
- Additional MS contributions to the overall budget of the WF should not exclude MS co-funding of individual projects
- Additional MS contributions introduce an element of flexibility to the future WF: if it is successful and running out of funds, it could be supplemented. If, on the contrary, the WF disappoints expectations, co-financiers could hold back and the sums at stake would be less.
- However, the Commission may use the co-financing option as a reason to reduce the resources allocated to the WF from the intra-ACP funds.
- Bilateral agencies’ co-financing of the WF should not be at the expense of their commitments to W&S from regular programmes.

5.3. *How should the WF operate?*

Assuming the WF continues, with or without co-financing from MSs, a thorough independent review of its policies and modalities will be necessary. An independent mid-Term Review is proposed to be carried out during 2007. Without prejudice to the findings of this review, the following proposals could be considered:

- i) It is taken as a given that:
 - the WF would continue to operate under EDF procedures;
 - a Brussels-based WF Unit would continue to have the main administrative responsibility for the Facility;
 - Delegations would be involved in its administration, suitably reinforced with additional resources;
 - the challenge fund concept would continue – with the modification proposed below:
- ii) WF should target:
 - W&S service delivery,
 - governance, strategy and capacity building in the water sector
 - *smaller* items of infrastructure and networks – avoiding duplication with donors and IFIs in funding major infrastructure.
- iii) The challenge fund structure should continue except for work in the areas of governance, strategy and capacity building, for which it is considered unsuitable.

- iv) Direct agreements should continue, using WF funds to subsidise international networks, international river basin agencies and other bodies which are consistent with its aims, and which do not receive adequate support from elsewhere.
- v) Revisit the original innovative mission of the WF: how feasible is it, in the light of experience with the WF so far, to encourage new modes of service delivery, technology, financing sources and structures, management systems and partnerships – and how can this be done?.
- vi) Review the principle established by the EU Council that the Water Facility "should not provide the majority share of funds for individual investment and private sector projects". Consider whether co-financing is an essential element of the innovative nature of the WF and whether co-financing requires additionality rather than simply complementing other available sources.
- vii) Schedule more frequent Calls for Proposals, each of a smaller size than at present (with shorter timetables for the decision cycle)
- viii) The upper and lower (Euro) limits for applications should be reviewed for each of the three categories in the light of other proposed reforms, and because of concerns expressed by NGOs and others.
- ix) Foster a more effective link between the ACP representation and voice on the Selection Panel and the regional and continental bodies such as AMCOW, AU-NEPAD
- x) Supplementing the capacity of Delegations to evaluate Proposals and subsequently to negotiate contracts and deal with other aspects of implementation of the WF.
- xi) Pro-active efforts by the Commission and Delegations as well as EU MSs and their in-country offices to raise awareness of the WF and stimulate demand for its funds in countries, and among groups, considered to be particularly needy.
- xii) Limit the eligibility of UN and other international specialised agencies as sponsors of bids.
- xiii) A protocol of cooperation should be concluded with the AfWF to avoid competition and overlap (e.g. concentration on projects of different sizes), and with the aim of defining a division of purpose.
- xiv) Promotion of the WF amongst local private water providers, banks and microcredit agencies, and other potential local interested parties at present under-represented amongst applicants (as proposed in the COWI report).
- xv) Technical assistance could be made available to sub-sovereign bodies (e.g. municipalities) for the preparation of Proposals – provided this could be done in an open and even-handed way (possibly with support from MSs, following on from existing initiatives).
- xvi) Review of previous good but unsuccessful applications to consider their potential for financing before the launch of future Calls.
- xvii) Evaluation criteria and information requirements of bidders should be reviewed in the light of the experience of the First and Second Calls for tender and in view of NGO complaints about possible bias against remote and rural projects. E.g. selection criteria on cost-effectiveness should not discriminate against target groups unable to demonstrate economies of scale (e.g. in isolated rural areas).
- xviii) In view of the conclusions of the recent EC Thematic Evaluation of the Water and Sanitation Sector for EuropeAid, the impact of projects on women and children should receive more weight as a criterion of selection.
- xix) The WF Unit could be supplemented by the appointment (including secondment from MSs) of a specialist in sub-sovereign, local and innovative water finance.

Annex 1. Key documents consulted

ACP-EU Water Facility:

“Lessons learned for applicants of the ACP-EU Water Facility First Call for Proposals”;

“Progress Report” Oct 2006;

“Newsletters” (monthly)

COWI A/S: *Examination of potential of the ACP-EU Water Facility for encouraging increased and innovative financing in water and sanitation.* August 2005

Development Initiatives: *Glass half empty: Europe’s response to the urgent needs of the poorest for clean water.* Prepared for WaterAid and Tearfund, Dec 2005

European Commission: *Thematic evaluation of the water and sanitation sector. Synthesis Report, Vol 1.* For EuropeAid July 2006

European Commission: *Communication from the Commission to the Council and the European Parliament: Communication on the future development of the EU Water Initiative and the modalities for the establishment of a Water Facility for ACP countries.* 26.01.2004

Hirsch, Danielle, “EU Water Facility: an opportunity to address the financing of water in innovative ways” Both ENDS, Bonn.(date unknown)

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UNDP: *Human Development Report 2006: Beyond scarcity: power, poverty and the global water crisis.* Palgrave, 2006

WaterAid & Tearfund: *An empty glass: the EU Water Initiative’s contribution to the water and sanitation Millennium targets.* Dec 2005