

LEGAL CHALLENGES TO IMPROVE AND REFORM THE PRIVATIZED WATER SERVICES IN INDONESIA

Dodik Setiawan Nur Heriyanto

Abstract: *Providing opportunity to the private sector to control water management system led to complications. However, such control has been authorized by the national law of Indonesia under the influence of the World Bank during the 1998's crisis. This study explores two important conclusions: first, civil litigation against the private water sector should be an urgent legal step in order to improve the quality of water services. Second, in accordance with the spirit and philosophical meaning of water as a nation's welfare asset under the 1945 Constitution, remunicipalization seems to be a suitable way to reform Indonesian's water management control system.*

Keywords: legal efforts, privatization, water management, civil litigation, remunicipalization.

Introduction

Having the world's fourth largest population, Indonesia has enormous responsibility to take care of the wellbeing of all its citizens.¹ In order to provide clean and potable water, Indonesia trusted the water management system to the private sector. This water privatization process is regulated by the Law no. 7 of 2004 on Water Resources. This law authorizes local governments to conduct the privatization of water services through local regulation. As a consequence of the dominant private control in the water services sector, public health is at stake. There have been multiple fact finding reports about the inadequate quality of services and the bad quality of the water. Through analyzing normative and comparative legal approaches, this study found that privatization dictated by international influences during the economic crises was the root of the water services

Dodik Setiawan Nur Heriyanto, PhD candidate at Faculty of Law, University of Debrecen and Lecturer at Faculty of Law, Islamic University of Indonesia.

E-mail: dodiksetiawan@uii.ac.id

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problem in Indonesia. Moreover, this study also propounded effective ways to reduce past, recent, and upcoming water problems.

1. International Influence as a Core Element of the Water Problems in Indonesia

The privatization of the water services sector in Indonesia started in 1990 when the World Bank provided financial assistance to Indonesia in order to build water infrastructure in the country. With the help of the World Bank's loan, Thames Water Overseas Ltd. (a London based company) in partnership with Sigit Harjojudanto, one of the sons of Suharto (the second Indonesian President), and Suez Lyonnaise (a France based company) in partnership with Salim Group (owned by Anthony Salim, Suharto's crony) ran Jakarta's water system by dividing Jakarta's water management system into two equal parts for each partnership (Robles, 2007, 56.). The influence of the World Bank lasted until 1998 when the economic crisis resulted in the state budget's financial collapse and led the Indonesian government to adhere Policy Reform Support Loan issued by the World Bank with the debt amount of altogether 2.5 billion US\$.² As a consequence of this, Indonesia must have complied structural adjustment programs of policy, institutional, regulatory, legal, and organizational reforms in the management of water resources and the irrigation sector under the World Bank's Water Resources Sector Adjustment Loan (abbreviated as WATSAL) (World Bank, 1999).

To implement the adjustment under the World Bank's conditions, Indonesia promulgated Law no. 7 Year of 2004 on Water Resource. This law reformed the substantial policy in water management and shifted it from government control to private management. Under this law, private sector enjoys tradable water rights (*hakgunausaha air*)³, the right to develop and manage the potable water system⁴, and to use the water resources for certain purposes in cooperation with state/locally owned enterprises.⁵ The World Bank concluded that the provisions promoting privatization of water services under the new law ensured good climate for infrastructural provisions and investments creating stable economic development (World Bank, 2004, 5-6.). However, this new law brought independent activists into

² The Bank's *policy-based lending* to Indonesia is closely coordinated with the overall reform agenda that is underway with support from the IMF, ADB, Japan and our other development partners. There have been four adjustment loans to date: (a) The first *Policy Reform Support Loan (PRSL)* - \$1 billion (approved and declared effective on July 2, 1998); (b) *Policy Reform Support Loan II (PRSL II)* - \$500 million (approved May 27, 1999 and made effective on June 17, 1999); (c) *Social Safety Net Adjustment Loan* - \$600 million in two tranches (approved May 27, 1999 and to become effective in the last week of January, 2000); and (d) the *Water Sector Adjustment Loan* - \$300 million in three tranches (approved May 27, 1999, effective and first tranche released in June 1999). See Indonesia: Macroeconomic Update (2000),

<http://siteresources.worldbank.org/INTEAPHALFYEARLYUPDATE/Resources/550192-1101735670271/indonesia.pdf>, accessed October 12 2015.

³ Indonesian Law No. 7 Year 2004 on Water Resources, art. 9 (1).

⁴ *Ibid.*, art. 40 (3).

⁵ *Ibid.*, art. 45 (3).

the streets protesting against the privatization of water services on the grounds that it would result in worse access to clean water in poor communities and, therefore, higher costs must be paid for the water.

After the enactment of Law no.7 of 2004, there has been a growing trend in the privatization of water services at regional levels. In 2004, the Government planned to privatize 250 Indonesian Local Water Utility Companies (*Perusahaan Daerah Air Minum*) in 27 provinces using the World Bank's financial support (Wignyosukarto, 2005). Such privatization mechanisms are regulated by local law as provided by Law no. 7 of 2004.⁶ Factual evidence proves that after the privatization, water management problems got bigger and more complex: higher water tariff than in the neighbouring countries (Indonesia: 0.7 US\$/m³, Singapore and the Philippine: 0.35 US\$/m³, Malaysia: 0.22 US\$/m³, and Thailand: 0.29 US\$/m³)⁷ and the fact that only 47.71% of Indonesian citizens get access to clean water (Direktor at Pengkajian Bidang Sosial dan Budaya, 2015, 51.). Moreover, in the upcoming years climate change and the growing number of people are predicted will most likely support the water deficit factor (Indonesian Ministry of Environment, 2015).⁸ If it does happen, then social conflicts generated by the water crisis could be unstoppable (Arsyad & Rustiadi, 2008, 95-96.; Green, 2002; Indonesian Ministry of Environment, 2014).

2. Legal Efforts to Overcome the Water Problems

In order to solve the complicated water problems in Indonesia, two suggested options may be feasible: overcoming poor services provided by the private sectors through civil litigation, and reforming the national concept for water management systems from privatization paradigm into the 'remunicipalization' concept.

2.1 Urgency to enforce the private sector through civil litigation

After having analyzed government's actions to overcome the water problems, we must conclude that these instruments are not capable of solving the water management problems through fast and fair settlement. Even though there was a renegotiation contract in 2001 between the locally owned company PDAM DKI (Jakarta) and its private partner (PT. PAM Lyonnaise Jaya (France) and PT. Thames PAM Jaya (England) (Hadipuro & Ardhianie, 2011, 1-3.; Koalisi Rakyat untuk Hak atas Air, 2011), water

⁶ Indonesian Law No. 7 Year 2004 on Water Resources, art. 16, 17, and 18.

⁷ Water tariff in Jakarta is 7.200 IDR (similar 0.7 USD) per cubic meter ranked as the highest charge in South East Asia and water quality is still questionable. Compare with other ASEAN countries, with only tariff charge 0.35 USD/m³, water in Singapore is drinkable. See Expert (2015): Water Tariff in Jakarta Highest in South East Asia (2015), <http://en.tempo.co/read/news/2015/01/11/057634142/Expert-Water-Tariff-in-Jakarta-Highest-in-South-East-Asia>, accessed October 20 2015. Tarif Termahal Se-ASEAN, Kualitas Air Murah (2010), <http://news.detik.com/lapsus/1292196/tarif-termahal-se-asean-kualitas-air-murahan>, accessed 20 October 2015.

⁸ Indonesian Ministry of Environment predicts that in 2025, there would be no enough clean water supply because of unresolvable of water management problems.

tariffs still remained expensive and not accessible to poor communities.⁹ So far, the numerous protests claiming responsibility of the service providers did not make the government to provide an efficient response. Apparently, the insufficient rules of business accountability and transparency drive providers in the private sector to focus on gaining profit rather than developing the quality of their poor services.¹⁰ Nonetheless, Law no.7 of 2004 shows a clear legislative effort to overcome the water management problems: people could start lawsuits based on the poor quality of water services that have an adverse impact on their life.¹¹

Instead of demonstrations, civil litigation would obtain the government's attention. Lawsuits also have legislative support under Article 82 (f) of Law no.7 of 2004, and various reports also reveal the poor quality of water services in Indonesia. A recent lawsuit was brought by KMMSAJ, the Coalition of Jakarta Residents Opposing Water Privatization in order to terminate the contract between PAM JAYA and its private partner. The District Court of Central Jakarta accepted their claim in 2015 and declared all agreements (including the amendments) between PDAM DKI and its private partner null and void.¹² Subsequently, the government that was one of the defendants in the case recently appealed against this decision. The majority of people argue that the government's appeal proves their unawareness of the water problems.

The civil lawsuit against the privatization before the Central Jakarta District Court could be a precedent for other similar actions to make providers in the private sector manage a better local water management system. In accordance with the Law no. 7 of 2007, all agreements on privatization of local water services that cause adverse impact to the local community must be terminated through civil litigation, and/or water services clients could even claim monetary compensation¹³ for the poor water quality that had caused health problems.¹⁴ After private sector providers realize that their poor services could be challenged in Court, they would probably pay more attention in order to develop the quality of their services.¹⁵ Litigation however is a last resort. In order to avoid civil lawsuits, the central and local governments should review their privatization policies.

⁹ See *Supra* note 7.

¹⁰ Study found in 2013 that 174 from 350 or in amount 50% of local water companies reported in giving unsatisfactory service. Indonesian Ministry of Public Work (2013), Daftar Kinerja PDAM, 2013, http://www.bppspam.com/index.php?option=com_content&view=article&id=652&Itemid=98, accessed October 26 2015.

¹¹ Indonesian Law No. 7 Year 2004 on Water Resources, art. 82 (f).

¹² Central Jakarta's District Court No. 527/PDT.G/2013/PN.JKTPST, 24 March 2015.

¹³ Indonesian Civil Code, art. 1365 (Every illegitimate act, which causes damage to third parties obliges the party at fault to pay the damage caused).

¹⁴ Less quality of water in big cities are one of the reason of degradation of public health in Indonesia. University of Indonesia Center for Health Research, *Survei Rumah Tangga Pelayanan Kesehatan Dasar di 30 Kabupaten di 6 Provinsi di Indonesia 2005*. USAID - Indonesia Health Services Program, Jakarta. 2006.

¹⁵ Most of private sectors serve in big cities other than DKI Jakarta, the capital city of Indonesia.

2.2 Remunicipalisation

Encompassing water management services through privatization indeed led to more disadvantages¹⁶ than the expected positive outcomes (Chinn & Web, 1987, 39-41.). The local governments are having authority to privatize water management services often support their decision of privatization with the idea of expected cost savings, while this initial cost saving dissipates overtime, especially where there had been limited competitive bidding in the first place (Gormley, 1991, 308-309.). Moreover, the objective of privatization, serving community interest, has been only a secondary interest of the privatized enterprises (Langmore, 1987, 44.). Several studies found that there was ‘no-social justice’ in privatized water services (Mulreanyet, 2006, 29-31.): increasing prices and the lack of guarantees to provide access to poor communities.¹⁷

Considering the actual disadvantages of privatization, this study recommends the government, both central and local, to dissertate a ‘remunicipalization’ policy in water management services. There have been success stories in several cities –in Paris (France), Dar es Salaam (Tanzania), Buenos Aires (Argentina), Hamilton (Canada), and some Malaysian municipalities (McDonald, 2012, 18.). The French water remunicipalization management system intended to tear inequality that the rich pay for the poor (Barraqué, 2003, 200.). Financially, there were significant direct savings for most municipalities – some 35 million Euro in the first year of the remunicipalization in Paris, and about 6 million CAD in the first three years in Hamilton – some of which were realized immediately after the profit taking for private management fees had been removed (McDonald, 2012, 13.).

Remunicipalization would preferably be suitable and may work very well in Indonesia in the water management sector. This idea can be supported with three important reasons:

- 1) Remunicipalization reassures the implementation of article 33 paragraph 3 of the Indonesian Constitution: “the land, waters, and natural resources within shall be under the powers of the State and shall be used to the greatest benefit of the people”. In contrast, the privatization of water services is clearly against the aim and spirit of the Constitution. A study found that remunicipalization typically improved access and quality of water services (PSIRU, 2014). Public management through remunicipalization of water will confidently protect the aim of the Constitution.
- 2) In accordance with the first reason, the Constitutional Court provides a conditional interpretation of article 33 paragraph (3) of 1945 Constitution in correlation with water management under Law

¹⁶ See *Supra* note 12.

¹⁷ Bayliss explains that privatization has had a negative impact for poor in terms of unemployment, decrease in income, and reduced access to basic services. Bayliss, K. (2002). *Privatisation and Poverty: The Distributional Impact of Utility Privatisation*. *Annals of Public and Co-operative Economics*. 2002, 73 (4) 603, pp. 603-604. See also Birdsall, N. & Nellis, J. (2002). *Winners and Losers: Assessing the Distributional Impact of Privatization*. *World Development* 1617. 2002, 31 (10), pp. 1618-1620.

no.7 Year of 2004.¹⁸ The Constitutional Court declared five restrictions on the interpretation: first, any concession on water must not violate the people's right to get water, therefore it must be controlled by the state and intended for the greater welfare of the people. Second, the state must ensure the people's right to water because access to water is a basic human right. Third, the use of water should be based on environmental sustainability. Fourth, the state has absolute nature to supervise and control the water sector because water is an important branch of production and serves the people, therefore it should be owned by the state and used for the people's welfare. Fifth, the main priority of the public enterprises and locally owned enterprises in is to engage in water concessions as a continuation of the right of the state to control the water and it is related with people's wellbeing.¹⁹ Changing the paradigm of Law no.7 of 2004 from privatization to remunicipalization would conditionally meet the five interpretations of the Constitutional Court. Therefore, amendment of the law is necessary and legislators must take remunicipalization into consideration when doing so.

3) After experiencing two financial crises in 1998 and 2008, the Indonesian economy recently recorded a relatively strong growth, and this firm pace of economic expansion has been accompanied by reduced output volatility and relatively stable inflation (Elias & Noone, 2011). Moreover, Indonesia has paid all of its debt obligations to the World Bank and IMF, and it is becoming an active member of IMF, and assigned a quota in IMF (IMF Rankles Again, 2015; Polemik Utang IMF, 2015). According to his, Indonesia has no further obstacles to change its policy to remunicipalization turning water management back into an area of public municipal managements.

Conclusion

Privatization scheme under the Law no.7 of 2004 led to unbalanced situations and disadvantages. Factual researches found that the privatized water sector created higher water tariffs compared to the neighbouring countries, and more than 50% of the Indonesian citizens do not get proper access to clean water. This evidence is in contradiction with the spirit of the principle that declares water as '*res communis omnium*' that should be under the power of the state that must use it for the greatest benefit of the people as it is ordered by the Indonesian Constitution. Therefore, legislative efforts must be taken in order to maintain the real purpose of water services under the Constitution: first, it is urgent to enforce the private sectors' better performance through civil litigation. Supported by Law no. 7 of 2007, all agreements on privatization of local water services that cause adverse impact to local communities must be terminated through civil litigation,

¹⁸ Constitutional Court Judgment No. 85/PUU-XI/2013.

¹⁹ *Ibid.* pp. 138-139.

and/or water services clients could even claim monetary compensation for the poor water quality that had caused health problems. Second, adopting the system of remunicipalization for water management services would effectively solve adverse water problems. The remunicipalization system has a purpose that meets the spirit of the Constitution, and since the IMF and the World Bank have no more dictates to Indonesia, we feel that this is the right time to place the water services back under public control.

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