

*Background paper*

## **Water financing and investment**

### *Introduction*

The purpose of the EU Water Framework Directive (WFD) is to ensure that a sufficient quantity of good-quality water is available for people's needs and the environment. Unfortunately, so far the WFD target of reaching good ecological status is achieved for less than 50% of surface water bodies in Europe, with the remainder still in poor ecological status.

To achieve compliance with the EU water acquis a significant financial effort will be required. These investment needs are generally driven by regulatory requirements, ageing infrastructure, economic development, demographic changes and new challenges such as climate change or emerging pollutants.

The benefits of investments in clean water accrue to society as a whole. They include a cleaner environment and invaluable ecosystem services, but also more narrowly defined economic benefits such as economic growth and increased competitiveness<sup>1</sup>. Water investments can also lead to avoided costs. Reducing leakages in the drinking water network for example can significantly contribute to energy savings and GHG emission reductions. Investments to avoid floods and droughts, or mitigate their impacts could also limit damage to economic assets.

### *Challenges*

➤ *Further efforts are hampered by structural levels of underinvestment*

The EU water sector is characterised by structural levels of underinvestment. According to the European Investment Bank (EIB), investment needs in water security and flood risk management amount to EUR 15 billion per year, while only EUR 2 billion are actually invested. In addition, investment needs to upgrade and renew the EU's water and wastewater systems are estimated at EUR 90 billion per year, while currently investments only account to EUR 30 billion per year<sup>2</sup>.

There are many factors that lead to underinvestment in water resources. Next to increasing pressure on public budgets – which is a challenge for most investments in public

---

<sup>1</sup> OECD (2016) “Water, growth and finance: policy perspectives”

<sup>2</sup> European Investment Bank (2016) “Restoring EU competitiveness: 2016 updated version”

infrastructure – water investments are hampered by the public good nature of the benefits of water services. In some cases it can be complex to clearly identify the beneficiaries of water services, which makes it difficult to make them pay for the provision of such services and consequently to offer an acceptable risk-return profile to potential investors. And even when charges are in place, cost recovery is often incomplete, which may lead to a vicious circle of underinvestment, resulting in inadequate maintenance of the infrastructure. This may lead to deteriorating service quality, which may decrease beneficiaries' willingness to pay etc<sup>3</sup>.

- *Article 9 of the Water Framework Directive requires Member States to recover the costs of water services, yet implementation could be further improved*

Article 9 of the Water Framework Directive requires Member States to take into account the principle of cost recovery of water services, including environmental and resource costs, in accordance with the polluter pays principle. Member States must put water-pricing policies in place that provide adequate incentives for users to use water resources efficiently.

However, based on the 1<sup>st</sup> River Basin Management Plans the European Commission noted that the implementation of Article 9 still had to reach its full potential. Only a number of Member States had changed their water pricing policies and very few had implemented a transparent recovery of environmental and resource costs<sup>4</sup>.

Preliminary conclusions from the ongoing assessment of the 2<sup>nd</sup> River Basin Management Plans suggest some progress on the rate of financial cost recovery, the number of water services to which it is applied and the consideration of environmental and resource costs. However, there is often still a lack of transparency about the calculation of cost recovery, in particular for environmental and resource costs.

---

<sup>3</sup> European Environment Agency (2013) “Assessment of cost recovery through water pricing” – EEA Technical Report no 16/2013

<sup>4</sup> European Commission (2012) “Commission Staff Working Document accompanying the Report from the Commission to the European Parliament and the Council on the Implementation of the Water Framework Directive (2000/60/EC) River Basin Management Plans” – SWD(2012) 379