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Corporatization of Public Water Utilities

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A more enduring model of reform is to transfer assets and liabilities, staff and the ongoing business of the utility into a corporation. This is known as "Corporatization". The entity would have a separate shareholding, board of directors and accounting and reporting lines. It may also be helpful as a first step towards private sector involvement. It is a process similar to this that was followed prior to Privatization in a number of jurisdictions.

Corporatization - Key Features

Corporatization has the following key features:

- **Separate legal entity** - the organization is legally established as an independent entity and hence the transfer of control is more durable than under utility reform.
- **Managerial autonomy** – management has virtually complete control over all inputs and issues related to production of services.
- **Transparency and reporting** - the utility is likely to become subject to prevailing company law and accounting rules in the country.
- **Assets and Liabilities** - the corporatized utility will have transferred to it the assets and liabilities appropriate for it to perform its functions and to be viable. It may be that it is inappropriate to transfer

all existing debt associated with the service to the corporatized entity if the utility is unlikely to be able to raise revenues to service the debt and fund existing operations. If a government wants a flourishing utility post-corporatization, it may have to assume or right off a substantial proportion of such debts. Assets and liabilities should also be correctly valued to avoid allegations (particularly if any part of the entity is divested at a later date) that there has been an undervalue, or public property is being given away, etc.). One element of assets which can prove contentious is what to do with receivables, particularly those owed by public entities. A sensible bad debts policy needs to be adopted with only those receivable which have a realistic possibility of recovery being transferred to the new entity.

- **Public law and private law** - in many countries public entities are subject to a body of law and court system known as administrative law and the administrative courts, which is different from that applicable to private citizens and companies. Corporatization of a utility may result in the utility becoming subject to private law - this is not always the case, however, even where the utility is incorporated into a limited liability company as it may still be deemed to be providing a "public service" and so the position should be verified with local counsel.
- **Board of directors** will represent shareholder interests but will also have fiduciary duties to the utility's wellbeing and potentially to other stakeholders such as customers and creditors.
- **Staffing** - It may be possible for the utility to follow different recruiting and staffing rules from the civil service rules, allowing for workforce benefits such as performance incentives and bonuses, together with more flexibility on hiring of staff and disciplinary procedures. Care will need to be taken to ensure that any increase in salary is linked to improvements in performance. Redundancy law issues regarding public employees will need to be taken into account. Any benefits currently available to staff will need to be examined to determine how these can be transferred. In the case of pensions, care will need to be taken regarding any pensions fund that has been built up and what liabilities are being transferred.
- **Independent status** includes a hard budget constraint or financial "bottomline"— which makes the organization fully accountable for its financial performance—with liquidation at least theoretically being the final solution in case of insolvency.
- **Greater financial independence** – need to combine corporatization with reforms allowing for increased portion of revenue coming from sales (rather than budget allocation), increased possibilities for keeping and using extra revenue, as well as a hard budget constraint: allowing company to retain excess revenues, but is also making it responsible for losses.

Corporatization - Checklist of Issues

Below is a checklist of issues to consider when contemplating Corporatization:

- Is new entity to be separate legal entity or just separate unit of existing utility or municipality?
- What assets and liabilities are to be transferred? Will new entity be required to pay for or account for these assets? If so, how will assets be valued? Are receivables to be transferred.
- Existing contracts with third parties - will these need to be novated or transferred?
- Will entity be subject to civil service employment rules? Is it possible to give performance incentives to employees? What are rules regarding transfer and redundancy of staff? What is to happen regarding benefits, especially pensions?
- Will there be a performance contract between entity and utility – will this be enforceable?
- Where will entity get its revenues – from end users or government grant, etc.?
- Are tariffs or revenues from customers sufficient to sustain cost of operations and costs of improvements? If not, will there be subsidies - if so, who will supply subsidies?
- Will new entity be a public or private law entity?

Corporatization - Lessons Learnt

Corporatization has been adopted in a number of countries. Lessons learnt from Corporatization in different sectors around the world show that it must be carefully tailored to the situation in order to be effective in meeting the government's goals: [\[1\]](#)

- Organizational reform must directly and contemporaneously address labor issues—you cannot leave labor for later. Many of the most serious efficiency and performance problems are rooted here. For more, click on [Labor Issues](#).
- Institutional innovations can allow organizational reform to be applied to new areas. Unbundling can enable market forces to be brought to bear in many areas previously thought to be natural monopolies. For example, concessions can create competition “for the market” when competition in the market is not possible.
- Intermediate reforms of autonomization and corporatization are more institutionally intensive—they imply a more sophisticated role for government—because government must utilize indirect disciplining forces rather than simpler instruments of direct control (as in a budgetary organization) or market forces (as in a privatized organization).
- A supportive external competitive environment must accompany reforms in internal incentives. If this environment is not present, systemic reforms may have to be implemented before organizational reforms can work.

[\[1\]Innovations in Health Service Delivery : The Corporatization of Public Hospitals](#)

Useful Links

- [OECD Guidelines on Corporate Governance of State-owned Enterprises](#)
- [What Lessons Can We Learn from IEG Evaluations in the Energy and Water Sectors?](#)
- [Key Topics in Public Water Utility Reform](#)
- [Ways to improve water services by making utilities accountable](#)
- [Characteristics of Well Performing Water Utilities](#)
- [Models of Aggregation for Water and Sanitation Provision](#)
- [Using a Private Operator to Establish a Corporatized Public Water Utility: The Management Contract for Johannesburg Water](#)

Related Content

- [Water & Sanitation PPPs](#)
- [Approaches to Utility Reform](#)
- [Water and Sanitation Agreements](#)
- [PPPs in Irrigation](#)
- [Managing Non-Technical Losses and Theft in Utility Contracts](#)

- [Water & Sanitation Toolkits](#)
- [Gender & Water and Sanitation Projects](#)

Additional Resources

- [Contracting Tools for Non-Revenue Water Reduction](#)

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