

Development of waste water treatment in rural areas with the support of the Cohesion Fund's projects

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Summary

Pure water usually ends up as waste water, which must be treated before being discharged back to nature. The entire territory of Estonia has been declared an area sensitive to pollution, because the slow shift of the water in bodies of water caused by the low relief of the land favours the excessive sedimentation of nutrients. Over the years, industrial and household waste water and agriculture have polluted the Baltic Sea and the internal bodies of water and worsened their ecological condition. Unthreatened bodies of water account for merely 37% of Estonia's surface water.

Contrary to the largest cities, no significant investments have been made in improving the water management infrastructure in rural settlements over the last dozen years. The majority of rural treatment facilities are unable to cope with waste water treatment and need to be modernised or replaced. Waste water is leaking to the ground due to depreciated sewerage pipelines. The exposure of groundwater and surface water to untreated waste water may cause the spread of diseases among the population and the suffocation of bodies of water due to excessive concentration of nutrients. Good waste water treatment prevents such problems.

In order to protect public health and fulfil the environmental requirements of the European Union, Estonia must improve the treatment quality of both drinking and waste water and achieve an ecologically sound state in its bodies of water. By the end of 2010 waste water must be collected and treated in all settlements. Applications can be made for large-scale support from the European Union's Cohesion Fund for the construction of water management infrastructure.

The National Audit Office examined the work of state agencies and local authorities in launching the first water management projects financed through the Cohesion Fund during the 2004-2006 programme period of the European Union. Three projects – those for the Western islands, the Matsalu ecological reserve and the Emajõgi and Võhandu Rivers – were audited in terms of the success of their preparation and instigation and the sustainability of the water management systems developed as a result. The audit incorporated 63 local authorities and seven regions of water companies established by them.

Making the best use of the funding allocated to it from the Cohesion Fund has proven a challenge for Estonia, as it has little experience in instigating and administering investments on such a scale. Although a number of significant shortcomings were identified in both water management project funding applications and the organisation of the sector in general in the course of the audit, the National Audit Office recognises the effort made by the state in the rapid launch of these projects.

In the EU's new programming period of 2007-2013 the central role and responsibility of the Ministry of the Environment in launching the Cohesion Fund projects, making funding decisions, coordinating procurement and exercising supervision over the final recipients will increase considerably. It is important to learn from the past mistakes when initiating and implementing new projects. The National Audit Office hopes that the recommendations made in this report help the state to use the funds of the Cohesion Fund more effectively.

According to the National Audit Office, Estonia is unable to ensure sufficient waste water treatment in all settlements by 2010, which may result in infringement proceedings by the European Union. Waste water treatment supported through the Cohesion Fund's projects has not been organised in a sustainable fashion, with the price of water and sewerage not incorporating all costs and there being lingering uncertainty regarding the future administration of new structures.

Key findings

- Too little funding is planned for the improvement of water management systems. According to the calculations of the Ministry of the Environment, it will cost 18 billion kroons to bring waste water management in all settlements into conformity with European Union regulations between 2007 and 2013, but only 12 billion kroons is currently planned for the development of water management and waste treatment in this period (including Cohesion Fund and state and local

government funding). Furthermore, projects from the second Cohesion Fund programme period will not be completed in time to fulfil the obligations of the European Union's urban waste water directive by 2010.

- There are problems with the involvement of local authorities in instigating projects. If a local authority has no interest whatsoever in participating in a project, the Ministry of the Environment currently has no power to oblige them to do so. Several local authorities are unable to take part in projects as their ability to cofinance them (including through loans) is restricted. Some local authorities were poorly prepared for their involvement in projects, lacking, amongst other things, a public water supply and sewerage system development plan.
- There are shortcomings in both the financial analysis of projects and their technological solutions. Ineffectual applications and confusion in assessing environmental impact led to delays in launching projects: the reviewing of applications by the European Commission took longer and additional terms and conditions were placed upon funding decisions which the state would have to fulfil before the funds were allocated. The main causes of the shortcomings that were identified were the demanding timeframe of the European Union's budgetary process in launching projects and the lack of the necessary preliminary studies. It is the view of the National Audit Office that more thorough assessment of the applications would have helped to avoid a number of these shortcomings.
- The sharp rise in building costs felt as a result of the delays in the projects has increased the need for additional state financing. In the last couple of years, the cost of building tenders for the environmental sector has gone up by an average of 1.8 times. For example, the tenders received in response to the design and construction procurement for AS Matsalu Veevärk in September 2006 exceeded the project budget by more than double. It is calculated that an additional 2 billion kroons will need to be found between 2008 and 2011 to compensate for the increased cost of the six Cohesion Fund projects currently under way. As this amount cannot simply be covered either by increasing the contribution of local authorities or from the budget of the Environmental Investment Centre, the projects will have to be supported through the state budget.
- The organisation of waste water treatment in rural areas with the support of larger Cohesion Fund projects will not guarantee the sustainability of the sector, as not all costs are being taken into consideration in determining the price of water and sewerage services. As a result, the revenue earned from these rates will not be sufficient for renovation and modernisation in the future – for either those structures that existed prior to the Cohesion Fund project or those being built as part of it. Thus a situation could arise where the state will have to cover the cost of exchanging old and damaged equipment, since local authorities and water companies will not have generated enough money to do this themselves.
- The water companies that were audited are able to cope at a satisfactory level with the administration of water management projects, but none of them has developed a business plan meeting the necessary criteria in terms of how to guarantee the further management of public water supply and sewerage systems that have been created once a project has reached its conclusion. It is due to this lack of business plans that the water companies are relying on the financial analyses produced as part of the Cohesion Fund project applications, which, in the view of the National Audit Office, are often inaccurate. As such, the management of these structures may prove in future to be considerably more expensive than forecast. It also remains largely unclear who will use the equipment and provide its services to consumers once the Cohesion Fund projects are launched, and whether common prices will be established in a region or set by individual local authorities.

Main recommendations

To the Minister of the Environment

- By the end of 2007 to prepare and overview of the status of water management of local authorities and to assess Estonia's ability to fulfil the requirements of the EU by the prescribed time. In the overview, to analyse in which local authorities it will not be possible to bring water management into compliance with the requirements by the prescribed time and to decide to what an extent and from where to find money for these investments.
- To make a proposal to the Government to develop common principles based on objective grounds for compensation for the rise in the prices of water management projects, which can be attributed to the rise in construction prices, thereby consulting the water companies as well as the local authorities. If necessary, allocate additional funds to the projects from the state budget, forecasting it in the State Budget Strategy. Establishment of a common procedure helps to plan the expenditure of the local authorities and the state and to avoid one-off solutions after an increase in the prices of construction procurement.

- To initiate a legislative amendment, which transfers the role of approving the price of water supply and sewerage services from local councils to another agency in the area of government of the Ministry of the Environment, either already in existence or to be especially formed for that purpose. Establishment of the prices of water supply and sewerage services at the state level helps to ensure that the tariffs take all the expenses relating to the provision of the service into account and to avoid problems arising from the lack of the will of the local authorities to establish tariffs of the required size.

To the Minister of the Environment and the Minister of Finance

- To improve the operations of preparation of projects in such a manner that before making decisions to finance large-scale environmental projects, which require local government funding the applications would be submitted to the Ministry of Finance for approval. Furthermore, to ensure that in the course of the project the Ministry of Finance is provided with information about any changes in the obligations assumed by the local authorities.

The Ministry of the Environment and the Ministry of Finance sent an official reply and the Association of Estonian Cities sent its comments to the draft audit report.

In reply to the recommendation of the National Audit Office to draw up by the end of 2007 an overview of the status of water management of local authorities and Estonia's ability to fulfil the EU's requirements the Minister of the Environment finds that he has a general overview of the funds required for the implementation of the directives and that it will be updated by the end of 2007. The Minister of the Environment finds that the local authorities must have an overview of the financial needs of rural municipalities.

Although the Minister of the Environment considers it important to compensate for the rise in the prices of water management caused by the rise in the construction prices, the Minister finds that it is difficult to develop common principles, because the capacity of the local authorities is very different. The Minister of the Environment finds that upon compensation of the rise in prices the capacity of the local authorities as well as that of the water companies must be taken into account. At the same time the Association of Estonian Cities considers it important to treat all local authorities equally upon covering the rise in prices.

The Ministry of Finance and the Ministry of the Environment find that it is not the state's duty to assess the financial capacity of the local authorities in implementing the Cohesion Fund projects, but the local authorities themselves should be responsible for it. According to both ministries, the coordination of water projects in the Ministry of Finance for the purpose of inspection of the financial capacity of the local authorities would take too much time. At the same time the Ministry of Finance has declared that it is ready to assess the financial capacity of the local authorities in the case the Ministry receives such an inquiry. The Association of Estonian Cities agrees with the recommendation to coordinate the project applications before making a financing decision with the Ministry of Finance, but also notes that it should be done quickly.

In response to the National Audit Office's proposal to transfer the role of approving the price of water supply and sewerage services from local councils to another agency, either already in existence or to be especially formed for that purpose, the Minister of the Environment confirmed that a legislative amendment is currently being initiated that is designed to resolve the problems associated with the establishment of water prices. However, the Minister did not specify how these problems will be resolved. The Association of Estonian Cities does not agree to any change to the competence of approval of water prices. The association recognises the potential for the price of water to rise, and draws attention in its response to the social problems this could lead to.

Although the Minister of the Environment recognises the same problems as the National Audit Office regarding the implementation of the Cohesion Fund water projects, the Minister finds that the Ministry of the Environment cannot carry out various recommendations because their implementation lies within the competence of the local authorities. For instance, according to the Minister, the recommendation not to allow the local authorities whose development plan does not contain an investment plan to participate in

the project, does not lie within the competence of the Ministry. The Minister of the Environment also found that he can only recommend that the local authorities include the methodology of pricing in the memoranda of association of the water companies.

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