

23 April 1998

The World Bank Inspection Panel

1818 H Street, N.W.

Washington, D.C. 20433

U.S.A.

VIA FAX: 091-202-522-0916

**c/o Judith Edstrom, Resident Representative, World Bank South Africa Mission,
Pretoria (HAND DELIVERED, SEALED ENVELOPE)**

**RE: Inspection Panel Claim regarding World Bank involvement in the Lesotho
Highlands Water Project**

To the Panel,

1. Introduction: Background

1.1 Introduction. We urgently request the Inspection Panel to investigate the World Bank's role in the Lesotho Highlands Water Project (LHWP) . This Panel Claim follows a submission made to you on 3 March 1998 by two civic associations in Alexandra and Soweto townships in Johannesburg, Gauteng Province, South Africa. That submission, which took the form of a letter faxed to your offices, was formally withdrawn on 20 April as a result of intimidation. However, the fundamental concerns over issues raised in the 3 March submission remain. As claimants, we are individual affected community residents of Alexandra whose signatures are on the attached page (but who wish to have our names held confidentially by the Panel) .

1.2 Intimidation on previous submission. The reason for our very late request, for which we apologize very sincerely, is that in the wake of explicitly clear South African government intimidation against going forward with the Inspection Panel submission -- which we can provide details about if the Panel requires -- the Alexandra community has been uncertain over how to proceed. The withdrawal was not based on any new, convincing information about the next stage of dam construction or its implications for low-income Gauteng communities, but rather on powerful political forces that operate in South Africa in a sensitive period just preceding the run-up to our country's second democratic election. We are providing you this information in the form of an Inspection Panel Challenge because, in our view, the underlying conditions that are generating pressure on low-income water consumers will only be exacerbated by allowing the LHWP to expand without the necessary studies about its impact and about alternative demand-side management approaches. While this Claim follows and expands upon many of the arguments put forward on 3 March -- for we have had access to similar technical information -- an additional point that requires mention is the incomplete study on the economics of delaying the LHWP, conducted by the Bank's LHWP task manager and released to the public in late March.

1.3 Community resolve to file Claim anonymously. We hereby request that the Inspection Panel urgently proceed with investigating our concerns as residents of Alexandra township adversely affected by the

LHWP, as laid out in this new Panel Claim. We ask that the Panel does so with the understanding that at this time we would rather remain anonymous in view of the chilling climate that now exists.

1.4 The LHWP. By way of background to the LHWP itself, concerns have often been expressed about design flaws associated with the first (completed) dam (Katse, Phase 1A). This Claim is based on the argument that "both Phase 1A and the next dam to be built -- Mohale (along with a diversion weir and tunnel to the Katse Reservoir), known as "Phase 1B" -- cause harm to the claimants and others similarly situated. Indeed we believe that a \$50 million World Bank loan for Phase 1B now being considered by the Executive Directors should be delayed until our concerns are addressed.

1.5 Original LHWP consultation with affected parties. The LHWP is the result of a 1986 treaty between the apartheid South Africa regime and a military regime in Lesotho that took power in a coup. By definition, hence, there was improper Bank consultation about the LHWP with these two states' citizens, many of whom in the mid-1980s were suffering imprisonment, torture and state-sanctioned murder for speaking out on behalf of democracy and development. This is not a theoretical issue, for during the 1980s the African National Congress formally opposed the LHWP. Under these circumstances, there was apparently no attention given by the World Bank design team to the concerns we have always had, in South Africa's impoverished urban townships, about the elimination of poverty, equity in resource allocation, universal access to water and water conservation. The result of not consulting was construction of a megaproject with many serious defects.

1.6 Recognition of flawed design process. The LHWP's legitimacy and the Bank's consultative process in project design have been called into question many times, and are beyond dispute. At an NGO conference on the LHWP in August 1996, for example, an official (Michael Potts) of the Development Bank of Southern Africa (DBSA) conceded, "Given the limited access to foreign funds by the South African government and the limitations on contractors' funding proposals -- export credit was not available to South Africa -- a very complex treaty was negotiated to bypass [anti-apartheid financial] sanctions. In Lesotho the credibility of the treaty was also questioned because the military government ruling Lesotho at the time did not permit open debate on the treaty." In short, according to even the DBSA official, "The planning of the social aspects of the LHWP was subordinate to the technical planning. The environment within which the environmental action plan had to be implemented was not conducive to sustainable development."

1.7 Other social and ecological issues raised previously. Concerns about the LHWP are not limited to consumer issues. At 185 meters, Katse is the highest concrete dam in Africa and one of the largest infrastructure projects in the world. Phase 1A directly affected 2,000 people -- approximately 300 households and indirectly affected at least 20 000 more who lost the use of common resources or income through the submersion of 925ha of arable and 3000ha of grazing land. This has had enormous social, environmental, and economic impacts on the people of Lesotho. Recent surveys indicate dissatisfaction on the part of Lesotho residents with resettlement schemes and provisions for reimbursement. Phase 1B will inundate 550ha of extremely good cropland and will force resettlement of 400 families. Following erosion of much of Lesotho's arable land over the past three decades, only 9% of the country's soil is presently available for cultivation. The proposed Phase 1B will exacerbate this situation, and in addition will destroy the habitat of the Maluti Minnow (an endangered species), bearded vulture and four other species considered "globally threatened."

1.8 Other implementation issues raised previously. Numerous complaints have arisen about the LHWP's implementation to date, including the lack of an initial Environmental Impact Assessment; a woefully inadequate social plan; flooding of ancestral burial grounds; an upsurge of social problems (including sexually transmitted disease and increased stock theft); poor labour relations that led to the murder of several workers by Lesotho police in September 1996; cost overruns due to an unanticipated need to line the Katse tunnels with cement; corruption on the Muela hydropower component of the project and funds established to devolve LHWP financial benefits to Lesotho's citizens; failure to account for soil erosion and sedimentation of the reservoir; and reservoir induced seismicity that in the village of Mapeleng generated a crack 1,5 km long that damaged nearly 70 houses. According to the leader of the Highlands Church Action Group, "The project shows no sensitivity to the impact on gender issues and roles of women." In addition, according to a leading academic at the University of the Free State, the effects on the Orange River catchment include a "considerable shortfall of water at the mouth... This will result in a river mouth that is either dry for years on end apart from exceptional floods or will be inundated by seawater intrusion." NGOs in Lesotho, South Africa and internationally have repeatedly brought these issues to the attention of World Bank staff (for example, at the 1996 conference and in continual correspondence between NGOs and the Bank LHWP task manager since)

1.9 World Bank role. The responsibility of the World Bank for social and ecological design problems, as well as the economic miscalculations described in more detail below, is also beyond dispute. The LHWP was initially funded by the World Bank with a US\$110 million loan on condition that South Africa stood surety. The Bank has repeatedly stated that its work on this project is small (just 5% of total project costs), thereby somehow implying that it is less liable for project problems. However, the following description from the Lesotho Highlands Development Authority implies a much more critical role: "The World Bank acted as a catalyst to bring all the financing together... It is also working to ensure that World Bank guidelines on resettlement and social impacts are met. The World Bank has the capacity to advise on ensuring that adequate attention is given to sensitive environmental issues. The World Bank's involvement assures lenders that the Project is a worthwhile investment opportunity." Thus the World Bank's role in this project extends beyond its role as a financial partner.. The presence of the Bank provides the catalyst that allows the project to exist, and is supposed to provide guarantees of technical assistance and leadership on mitigation of social and environmental impacts. By rushing this project and requesting approval for financing from Bank Executive Directors before necessary studies and public participation have taken place, Bank staff are undermining the credibility of the institution and the LHWP, and, we argue, are causing material harm to the people of South Africa and Lesotho.

1.10 South Africans' financial obligations. Part of that harm can be measured in rands and cents. According to the Bank, "In terms of the Treaty, South Africa bears the full costs of the project as well as the associated debt, except for a hydroelectric component which will supply all of Lesotho's power requirements and which is being financed 100% by Lesotho with donor assistance. Lesotho bears none of the 'costs linked to the water transfer component of; the project.'" As Water Affairs and Forestry Minister Kader Asmal put it in a speech to the 1996 Group for Environmental Monitoring Workshop on the LHWP, "The debt related to the water transfer part of this project will be redeemed by South Africa through income generated by the project. In other words, the end users will pay for the project, at tariffs well within the capabilities of the beneficiaries, making it economically viable." This is the crucial point of debate, and we want to assert that, in hindsight, Minister Asmal -- and World Bank staff who have

advised him on water pricing, at retail level, for low-income residents of Gauteng townships are incorrect in this statement.

1.11 Relative water access by low-income consumers. Gauteng consumers bear the bulk of the LHWP costs, both for capital and recurrent expenditures. But millions of the province's low-income citizens are already beset by severe problems of poverty, disease, environmental decay, geographical segregation and women's oppression due to the inadequate levels and high costs of water and sanitation services. South Africa's inequality in access to water is striking. According to a recent Central Statistical Services Household Survey, only 27% of African households have running tap water inside their residences and only 34% have access to flush toilets. By consuming less than 2% of all South Africa's water, the country's black township residents together use less than a third of the amount used in middle- and upper-income swimming pools and gardens, not to mention white domestic (in-house) consumption or massive water wastage by white farmers who have had enormous irrigation subsidies over the years and who use 50% of South Africa's water. Moreover, out of every 100 drops that flow through Gauteng pipes, 24 quickly leak into the ground through faulty bulk infrastructure. Still more waste occurs in leaky communal, yard and house taps. In the higher elevations of Alexandra township, these problems are witnessed in the perpetual lack of water pressure. Hundreds of thousands of low-income people in Alexandra and other townships have no immediate house or yard access to reticulated water supplied by our Johannesburg municipality, and instead receive at best only communal access, with all the public health problems that this implies. Indeed, the lack of available water on a universal basis means that public health conditions are worse; geographical segregation of low-income Gauteng residents (from wealthier residents) is more extreme; women are particularly inconvenienced, and their income-generation and care giving capacities are reduced; and the environment is threatened (in part because of the shortage of water-borne sanitation) . For reasons established below, we believe that the LHWP expansion will exacerbate rather than ameliorate our access, equity and quality problems. This could not come at a worse time, as Gauteng municipalities - including Johannesburg -- are suffering extremely serious financial difficulties that are forcing them to dramatically increase the pace of water cut-offs to low-income consumers, as well as the retail price of water.

1.12 Alternatives not explored sufficiently. Are there alternatives to Phase 1B? Bank staff do not know, for as far as we can determine, the desire by communities to address our townships' own water-infrastructure shortcomings especially leaky connector pipes, but also leaky water taps that together cost Sowetans approximately 40% of our water -- has never been fully explored or supported by Bank staff. The possibility for changing water usage patterns through progressive block tariffs has not been factored in (in part because Bank staff explicitly oppose differential pricing of water). The impact of water conservation education has not been considered. The possibilities for regulations prohibiting excessive watering of suburban gardens has not been addressed by Bank staff. The potential for saving water through clearing invasive alien trees has not been calculated. The physical replacement or installation' of low-flow showerheads, dual-flush toilets, and similar mechanical interventions have not been addressed. These are crucial alternatives which could ameliorate the need for the remaining phases of the Lesotho project. These alternative options have not been taken seriously, as far as we can tell from analyzing Bank-supplied information.

2. The Inspection Panel Claim

2.1 Claimants as affected parties. As residents of Alexandra township, we are part of the low-income consumer population who must pay a disproportionate bill for the LHWP. As "affected parties," the claimants and others similarly situated have suffered and will suffer harm because of violations of Bank policies associated with LHWP Phases 1A and 1B, as outlined below. We live within the country or an area immediately affected by the Bank-financed project. Finally, through the contacts of our technical advisors, Non-Governmental Organisations here and abroad, community organisations in Alexandra with which we are allied, and more general public pressure and publicity, our concerns have been repeatedly raised with Bank management. We are not satisfied with the response, particularly in relation to the possibilities of combining demand-side management with universal access to water.

2.2 Summary of Claim. To briefly summarise our concerns, the LHWP represents an expensive, ecologically unsound water supply project whose expansion is not needed for many years (by some estimates, two decades) and that has resulted and will result in a variety of problems that represent material harm to the claimants and our allies:

2.2.1 rising water prices (thus adversely affecting the ability of low-income people to gain access to water, and in the process lowering public health status and environmental conditions, with particular costs borne by women, children and the elderly);

2.2.2 less incentive to instigate demand-side management measures (hence leaving townships with failing infrastructure and limiting the ability of service providers to cross-subsidise);

2.2.3 increased fiscal stress on municipalities (which in turn will cost workers their jobs and/or income, and will lead to greater pressure to reduce subsidies to low income people and to cut off water in the event of nonpayment); and

2.2.4 fewer resources for the capital and recurrent, subsidies required to improve and construct water supply infrastructure appropriate for low-income communities.

2.3 Phase 1B delay is feasible. Over the past six months, information has been presented publicly and privately by South African authorities as well as Bank staff, that lead us to conclude that a significant delay in further LHWP construction is not only possible but would save hundreds of millions of Rand per year (even considering the continuation of payments to Lesotho for water that would have been delivered with Phase 1B, and the economic loss to Lesotho if 1B was delayed). As stated by an official of Rand Water and reported in Johannesburg newspapers on 13 March 1998, "we could drop supply by 40%" and in the process delay the LHWP "by years," hence "conservatively" saving R800 million per annum. That money could be spent on demand-side management alternatives that would conserve water and assure equity.

2.4 Demand-side alternatives not yet investigated. We understand that Bank staff still have not required a full study of demand-side management alternatives before recommending a new LHWP loan, despite its own policies on Alternatives, Economic Evaluation of Investment Options and Water Resources Management, among others. Communications from Bank staff concede that demand-side management should have been studied in much greater detail at

the outset, but the concluding argument is that the project is "too far along" to make a delay economically viable. Despite requests and extensive publicity about the issue in the South African press, information or studies that would clarify the economic consequences of enhanced demand-side management have not been made available to us.

2.5 Shortcomings in Bank study on economics of a delay. The Bank's March 1998 study on the economics of a delay in the LHWP downplays the possibility of substantial demand-side management interventions. The new report assumes a 3.3% annual water demand increase in Gauteng, and therefore clearly does not take demand-side management arguments seriously. Specifically, the new study makes the following comments about demand-side management, which indicate a lack of serious consideration of the issues under debate: "It is not clear what the scope is for further demand management ... Demand management capabilities and their impact in South Africa are theoretical and have not yet been tried and tested... The last thorough analysis of water demand in the Vaal system was done in the mid 1980s."

2.6 Implications of proceeding too rapidly with Phase 1B. Thus we are concerned that the decision to proceed based largely on sunk costs ignores the significant economic benefit of demand-side management (thereby failing to seriously consider a viable and important alternative, in violation of several Bank policies). Bank staff seem intent on moving this forward despite clear and obvious problems and policy violations, and we question the incentive structure that appears to encourage Bank staff to throw good money after bad. Bank staff appear to be motivated to move money for the sake of moving money, rather than carefully considering the implications of moving forward with the project or the cost savings, social and environmental benefits inherent in a delay. We question the wisdom of throwing more money at a project when important questions about the need for the project exist. We also note that, as discussed more fully below, continuing with this project will have an enormous effect on South Africa's future water management planning.

2.7 Implications of delaying Phase 1B Than decision. A reconsideration of this project in accordance with the Bank's policies on environmental assessment, consultation, and consideration of investment alternatives would allow the parties concerned to save money and would give further incentive to South African state agencies -- at national, catchment-area and municipal levels -- to focus on steps that are consistent with the objectives of poverty alleviation and access to water for the poor. The authorities could take steps to fix the region's badly leaking delivery system, install water-conserving appurtenances, and implement measures such as tariff reform to reduce use by the biggest and most wasteful users. Otherwise, we believe this very costly project will force Rand Water --responsible for 18% of debt-service costs of the project -- to sell greater amounts of higher cost water. The requirement that Rand Water pays for the unneeded water will generate a strong disincentive for conservation. We believe that the Bank has failed to adequately consider the impacts that the project will have on South African consumers and the environment.

2.8 Delay of approximately ten months required. A delay in a funding decision is necessary until a demand-side management report is prepared, which is anticipated in early 1999. We understand there have been no public studies that document the economic impact on Rand Water of bringing this water on-line before it is needed. Given the inaccuracy of earlier Bank demand estimates (which were overoptimistic by a factor of 40%), the project's economic analysis could be profoundly affected by new information on demand. Moving ahead before the information is complete violates policies on

Economic Evaluation. To wait ten months for more scientific demand-side management studies would not, Bank staff concede in the study on the economics of delay, result in the withdrawal of favourable bids by construction companies.

2.9 Implications for retail water pricing and investment. Finally, the claimants are also concerned that the high cost of LHWP water will worsen the impact that follows directly from other Bank advice to the South African government regarding fiscal management, water pricing and infrastructure investment. The Bank's policy advice and the Bank's promotion of LHWP are integrally linked, as was demonstrated during an October 1995 presentation by Bank staff to a Department of Water Affairs and Forestry (DWAF) conference. At that conference, detailed water pricing principles contrary to those advocated by civic associations and even the main purchaser of LHWP water, Rand Water, were promoted during a Bank slide presentation on the LHWP, notwithstanding explicit suggestions to the contrary by civic movement representatives and Rand Water in consultations prior to the conference. Indeed the Bank's South African policy advice -- in the water sector for both urban consumers and low-income rural farmers (during the October 1995 conference and in subsequent communications with DWAF) and regarding infrastructure investment (the Urban Infrastructure Investment Framework of March 1995) -- has consistently contradicted the traditional civic movement demand, and constitutional guarantee, that water is considered a human right, and that a universal entitlement be provided. The Bank staff's advice is also opposite to that found in the 1994 World Development Report: Infrastructure for Development, and is fundamentally incompatible with the Bank's mission of poverty reduction, as discussed below.

2.10 Implications for municipal fiscal stress. Municipalities have borne the costs of rising water prices and limited retail affordability in recent months, and are passing them on to workers, who are increasingly suffering wage and retrenchment pressure, and to communities, in the form of increased levels of water cut-offs. This reflects both overall municipal fiscal stress (as central to local grants declined by 85% in real terms from 1991/92 to 1997/98) as well as higher priced bulk water costs. Debts by Gauteng municipalities for bulk sewerage and bulk water supplies that are more than 60 days overdue amounted to R69 million at the end of 1997, and another R20 million in water-related debts were between 30 and 60 days overdue. The 24 Gauteng municipalities raised total income of R968 million from water bills to all classes of consumers in 1997 and spent R1 019 million on water services (a deficit of R51 million). In contrast, of the 236 municipalities that report across South Africa, water bills raised R 2414 million in 1997, and expenditures were just R 2388 million (a surplus of R 26million). This is surprising given that Gauteng is South Africa's wealthiest province. The fiscal stress caused by deficits on the water account are part of the reason that the following Gauteng municipalities were declared, in December 1997, to be in default of government "viability" criteria (sufficient cash and investments to meet one month's personnel bill): Johannesburg, Pretoria, Alberton, Brakpan, Randfontein, Bronkhorstpruit, Walkerville and Vereeniging Koponong.

2.11 Implications for low-income residents. The direct consequence of rising indebtedness has been intensified municipal "credit control" against those households who can not afford to pay for increasingly costly water. Rand Water price increases announced in February 1998 - which were more than 50% above the inflation rate, because 75% of the increase is from the LHWP -- will affect the claimants at a time that unemployment is increasing, overall municipal bills are being increased and some Wealthy ratepayers are offering stiff resistance to paying their fair share. The implications of rising water prices and the lack of a "lifeline tariff" -- a basic water service available to even to the very poor -- include not

only switching of funds in household budgets away from other necessities, but also a dramatic increase in residential water cut-offs in Gauteng since early 1997. According to the Department of Constitutional Development's "Project Viability," 24 out of the 30 Gauteng local authorities (representing a population of more than 12 million people) that replied to an official questionnaire, engaged in water cut-offs. These cut-offs affected 512 households in the first quarter of 1997, 932 households in the second quarter, 1 210 households in the third quarter and 5472 households in the fourth quarter. The ability of many of these households to afford their bills was limited, as witnessed by the fact that only 252, 449, 613 and 1 064 Gauteng households were reconnected in those four quarters of 1997, respectively. There are many other potential indicators of the costs of increasing water tariffs associated with the LHWP, including public health costs and ecological problems (as excessive water-borne sanitation costs lead to informal sanitation arrangements), most of which generate a bias against low-income women, which should also be researched and factored into the water pricing and access policies. However, these are at present not being adequately considered, due to the intensive pressure municipalities face to balance their books in the very short term.

3. Contact with the World Bank

3.1 Contact with the World Bank. Prior to filing the Inspection Panel submission of 3 March, civic association leaders took the following steps to resolve differences with the World Bank:

3.1.1 initial discussions were held between Bank staff, South African National Civic Organization (SANCO) staff and Rand Water officials in September 1995, in which the civic position (endorsed by Rand Water) in favor of lifeline water supplies and cross-subsidies was recorded but formally opposed by Bank staff (indeed the civic position was specifically rejected by Bank staff during a October 1995 DWAF conference, in spite of lifeline supplies being recommended in the previous year's World Development Report as well as the ANC's Reconstruction and Development Program, which was its campaign platform in 1994 and hence its mandate to govern);

3.1.2 there was a subsequent identification and 'discussion of the problem of inadequate demand-side management analysis at an NGO consultation meeting (attended by a researcher who serves Gauteng civic organizations) at the World Bank in Washington, DC on 23 October 1997, where once again Bank staff rejected without serious consideration the position put forward on behalf of lifeline water supplies and cross-subsidies;

3.1.3 there were subsequently several e-mail requests to World Bank staff for information concerning the relationship of the LHWP to Bank policy advice on water pricing and tariffs, in October-November 1997;

3.1.4 several e-mail invitation letters and oral invitations were sent to World Bank staff (based in both Washington and Pretoria) in November 1997, to join 80 Alexandra and Soweto township leaders at--and present information to, and learn from a large workshop (on 16 November in Johannesburg), specifically about the IHWP and its implications for Gauteng communities (Bank staff did not attend, notwithstanding indications they would);

3.1.5 an e-mail letter was sent to World Bank staff on 26 November 1997, clarifying the position of the civic associations and requesting information on how to bring a Claim to the Inspection Panel;

3.1.6 an e-mail invitation was sent to World Bank staff to tour Alexandra township in December 1997 (the invitation was initially accepted but then rejected);

3.1.7 a public statement was made by many Non-Governmental Organizations concerning the need for a delay in Phase 1B on the occasion of the 20 January initial transfer of water;

3.1.8 there was a meeting between Alexandra and Soweto civic leaders and World Bank staff on 21 January 1998; and

3.1.9 a follow-up letter was sent to World Bank staff on 27 February 1998, specifying the civic movement's objections to the LHWP.

3.2 World Bank reactions. World Bank staff had private discussions with leaders of the Alexandra and Soweto communities, but it is disappointing that there was not direct Bank contact with larger groups of low-income Gauteng residents affected by the LHWP. Opportunities to visit the affected townships and meet their residents in order to experience firsthand the water problems were declined by Bank staff. The Bank also made public its responses to civic concerns through two newspaper articles' that appeared in Business Day: "Delaying water project 'would increase risk of severe shortages'," 5 February; "SA advised to proceed with Lesotho project," 25 March. Business Day is not, however, widely available within Alexandra township.

3.3 Inadequate response to concerns. The Bank's response to legitimate community concerns has, to date, been inadequate. The need for attention to the demand related issues raised is largely unmet, even though the Bank has enormous resources available to conduct demand-side management studies and make staff available for consultations with affected communities. The acknowledged lack of scientific demand-side management research conducted by the Bank is disturbing, particularly when considering the enormous cost implications for our region's consumers. Bank staff owe it to those paying the LHWP's bills to ensure that their research is water-tight, and that they have communicated this research to Gauteng consumers in a proactive manner.

4. Contact with the South African Government

4.1 Contact with the South African government. In addition to making concerns known to the Bank, additional steps were taken by civic leaders to address the problems within South Africa (prior to the withdrawal of the Inspection Panel submission on 20 April)

4.1.1 an initial statement of concern was made to South African authorities, in the form of a protest march from Soweto to the Johannesburg Southern Metropolitan Local Council over

dramatic increases in water bills (which were entirely attributed by Johannesburg councillors to the LHWP) on 22 July 1996;

4.1.2 a meeting /workshop with Rand Water was held on 16 November 1997;

4.1.3 a letter setting out these concerns was sent to Minister Asmal in January 1998, and a meeting was held on 6 March 1998.

4.2 Government support for Phase 1B. The South African Government has not responded with detailed studies as to whether Phase 1B can be delayed through a demand-side management strategy. It is possible that Minister Asmal may, over time, be successful in implementing more sensible water policies with a demand side management orientation. However in the short term, high levels of pressure from vested interests, including World Bank staff, appear to have generated an official South African Government decision in favour of proceeding with Phase 1B, notwithstanding documented opposition from technical experts employed by Rand Water. There has also been explicit intimidation by the South African government against the use of the World Bank Inspection Panel mechanism to help resolve the concerns. For these reasons, it is imperative that the Inspection Panel mechanism be brought to bear as a neutral referee.

5. Applicable World Bank Policies and Operational Directives

5.1 Relevant policies. The World Bank abides by numerous policies and procedures that may have been violated by the LHWP. These policies are applicable (though not universally) to Phase 1A as well as (universally) to the next phase of the project, Phase 1B, now under consideration by the Bank. The following are relevant policies which we believe were violated by Phase 1A (though some did not apply at the time 1A was constructed) and that will be violated by Phase 1B.

5.2 OD 4.00, Environmental Policy for Dam and Reservoir Projects (Consultation) Para 19. Consultation with Non-governmental Organizations (NGOs) and Affected Groups, states: "Community organizations, research centers, environmental advocates, and other NGOs can often provide valuable perspectives on improving both project design and implementation. To tap these perspectives, the Bank encourages consultations by project authorities (including consultants preparing the project) with appropriate NGOs, particularly local NGOs ... In addition, the Bank encourages consultation between project executing agencies and the population affected by the project, as part of the project design process."

5.2.1 As consumers and citizens who will have to pay for the LHWP, we have not had a truly adequate consultation with the Bank at any stage of this project, but the failure to consult more widely, notwithstanding opportunities presented to World Bank staff, is especially evident and problematic in light of the questions raised about demand-side management and project costs.

5.2.2 We believe it essential that civil society be brought into a public debate about the expansion of the LHWP, in part through a project delay. Because low-income water consumers have not been adequately consulted, we will suffer adverse consequences, including less access

to Government officials and lower consciousness of our conditions than would have otherwise been the case had Bank staff taken seriously their mandate in the area of consultation.

5.3 OD 4.00, Environmental Policy for Dam and Reservoir Projects (Design Alternatives). Para. 5, Design Alternatives, states: "Design of investment programs for supplying water or energy should consider demand management as well as supply options (e.g., conservation of water and energy, efficiency improvements, system integration, cogeneration, and fuel substitution)

5.3.1 The Bank has not fully investigated demand-side management options during the planning of either phase of the LHWP. As noted above, Bank staff have inadequately responded to findings relating to demand-side management, by failing to conduct rigorous evaluations prior to seeking further funding for 1B. It is possible that effective demand-side management could delay for many years the need for this massive project, and Bank staff's failure to consider this possibility seriously is a fundamental violation of Bank policy with considerable economic, social and environmental impacts. Moreover, the Bank's initial 1A demand calculations were terribly inaccurate -- 40% higher than actually occurred -- and it is worrying that scientific analysis associated with 1B-related water demand will not be available for some time.

5.3.2 Demand-side management in the townships has not been taken seriously by officials, for it is only now that attempts to address faulty, apartheid-era infrastructure are being made, and even now only in a tentative way without sufficient financial commitment. It is true that there are (very minor) financial commitments now being made in these areas, but in the context of municipal fiscal stress discussed above these are not likely to make a substantial difference. We are aware that the Bank has made its own contributions to South African debates over demand-side management, but in these contributions, Bank staff have overstressed financial (not economic) efficiency measures (through a proposed pricing system) and downplayed -- often even arguing explicitly against - entitlement access through the kind of lifeline tariff and progressive block tariff measures supported widely in South African townships, and endorsed in the World Development Report 1994 and the Reconstruction and Development Program. The latter document clearly specified the need for tariff restructuring, cross-subsidies and lifeline services to the poor:

- To ensure that every person has an adequate water supply, the national tariff structure must include the following:
- a lifeline tariff to ensure that all South Africans are able to afford water services sufficient for health and hygiene requirements;
- in urban areas, a progressive block tariff to ensure that the long-term costs of supplying large volume users are met and that there is a cross-subsidy to promote affordability for the poor, and
- in rural areas, a tariff that covers operating and maintenance costs of services, and recovery of capital costs from users on the basis of a cross-subsidy from urban areas in cases of limited rural affordability (section 2. 6. 10).

5.3.3 Similar points were also made repeatedly in the World Development Report 1994, though they were rejected by Bank staff operating in South Africa (both in the water pricing advice and in the Urban Infrastructure Investment Framework):

There are, however, ways in which infrastructure subsidies can be structured to improve their effectiveness in reaching the poor. For example, for water, increasing-block tariffs can be used -charging a particularly low "lifeline" rate for the first part of consumption (for example, 25 to 50 liters per person per day) and higher rates for additional "blocks" of water. This block tariff links price to volume, and it is more efficient at reaching the poor than a general subsidy because it limits subsidized consumption. Increasing-block tariffs also encourage water conservation and efficient use by increasing charges at higher use. These tariffs are most effective when access is universal. When the poor lack access, as is frequently the case, they do not receive the lifeline rate and typically end up paying much higher prices for infrastructure services or their substitutes (pp.80-81).

5.3.4 The Bank staff's acts of omission are having and will continue to have serious material, adverse consequences for low-income residents -- such as water cut-offs, water wastage and unhygienic conditions associated with leaky township water systems -- and will in the process exacerbate the dramatic inequalities between races and income groups inherited from the apartheid era.

5.3.5 As mentioned above, many design alternatives to the LHWP are now being seriously explored within DWAF. Yet various demand-side techniques have apparently not been factored into demand schedules or demand curves for the Vaal basin. They include repairing our townships' leaky connector pipes and leaky water taps, modernizing and fixing meters, changing water usage patterns through progressive block tariffs, promoting water-sensitive gardening and food production, intensifying water conservation education, regulating or prohibiting excessive watering of suburban gardens, implementing other water use regulation, clearing invasive alien trees, promoting school water audits, billing consumer with more informative material, and installing low-flow showerheads, dual-flush toilets and similar mechanical interventions. The Bank has the resources to -- and-should as a matter of policy -evaluate such. options, but in the case of both phases of LHWP, did not. In violation of Bank policies, alternative options have not been considered seriously.

5.4 OP 10.04, Economic Evaluation of Investment Options. Para. 3, Alternatives, states: "Consideration of alternatives is one of the most important features of proper project analysis throughout the project cycle. To ensure that the project maximizes expected net present value, subject to financial, institutional, and other constraints, the Bank and the borrower explore alternative, mutually exclusive, designs. The project design is compared with other designs involving differences in such important aspects as choice of beneficiaries, types of outputs and services, production technology, location, starting date, and sequencing of components. The project is also compared with the alternative of not doing it at all." Moreover, Para 5. Sustainability, states: "To obtain a reasonable assurance that the project's benefits will materialize as expected and will be sustained throughout the life of the project, the Bank assesses the robustness of the project with respect to economic, financial, institutional, and environmental risks. Bank staff check, among other things, (a) implementation to ensure that the project functions as designed, and 9b) whether critical private and institutional stakeholders have or will have the incentives to implement the project successfully."

5.4.1 There has been little or no analysis of how building either 1A from 1986-97, or building the proposed 1B now, before the water is needed, has affected and will affect Rand Water and its end-users, especially low income users with inadequate access to water or who suffer the effects of failing infrastructure. Analysis conducted to date does not sufficiently evaluate alternatives to 1B, by fully considering the costs and benefits -- including social and environmental benefits of not building the project. In short, Bank analysis regarding 1A was innocent of any of the economic and sustainability concerns we raise now, and analysis of 1B's optimum starting date has not seriously incorporated demand-side management possibilities, and hence is weighted toward funding and completing the project at the earliest opportunity. A more thorough analysis of 1B may reveal that a major delay is not only cost-effective but also desirable.

5.4.2 One important economic justification for building the project now is the possibility of a major drought. The detailed economic analysis of drought, and possible scenarios for dealing with it other than building this dam, have not been shared with affected communities. Whether demand-side management that could reduce the supply need by 40% would mitigate the drought costs has not been considered by the Bank. Moreover, the expansion of water storage (through Phase 1B's construction) beyond that presently required will have the effect of hindering conservation efforts, compared to the option of dam delay, thus exacerbating problems in the event of a drought.

5.4.3 The sustainability of Phase 1B has not been securely established, since a thorough study on its impacts on the downstream environment is not yet complete and will not be for a few years. The Orange River is already suffering from over-allocation problems downstream, and this project will add to that problem. Again, the Bank is proceeding with a project without considering the important social and environmental impacts of its actions, in violation of its policies.

5.4.4 This project is also not sustainable economically, due to the burden it will place on Rand Water and its end-users. To illustrate, according to 1995 Bank reports, a cubic meter of water from the Vaal Dam costs ..(in SA currency) 8 cents (US\$0,016), from Bloemhom 10 cents, from Tugela Vaal 21 cents, and from the combination of Lesotho's Katse (complete) and Mohale (proposed), a staggering R1,50 (US\$0,30). Bank staff have told Minister Asmal that it would be "economically appropriate" to raise the price of Vaal water from 30 cents to R1,50 per cubic meter. To put this in perspective, the three other projects provide Gauteng with 2,3 billion cubic meters a year, while the two Lesotho dams together would add just another billion. There has been no published information on whether the economy of Gauteng can absorb such price increases.

5.5 OP 4.07, Water Resources Management. Para. 1 states: "Bank involvement in water resources management entails support for providing portable water, sanitation facilities, flood control, and water for productive activities in a manner that is economically viable, environmentally sustainable, and socially equitable." Moreover, Para. 2 states: "The Bank assists borrowers in the following priority areas: (a) Developing a comprehensive framework for designing water resource investments, policies and

institutions. Within this framework, when the borrower develops and allocates water resources, it considers cross-sectoral impacts in a regional setting (i.e. a river basin). (b) Adopting pricing and incentive policies that achieve cost recovery, water conservation, and better allocation of water resources. (c) Decentralizing water service delivery, involving users in planning and managing water projects, and encouraging stakeholders to contribute to policy formulation. The Bank recognizes that a variety of organizations 'private firms, financially autonomous entities, and community organizations may contribute to decentralizing water delivery functions. Thus it supports projects that introduce different forms of decentralized management, focusing on the division of responsibilities among the public and private entities involved. (d) Restoring and preserving aquatic ecosystems and guarding against overexploitation of groundwater resources, giving priority to the provision of adequate water and sanitation services for the poor."

5.5.1 Because the LHWP will result in water cost increases (9% this year, following a 30% increase last year) of above the inflation rate (last year below 8% and presently below 6%) for poor users (according to Standard and Poors analysis of Rand Water, and-in a press conference on 27 February, according to Rand Water itself), and because it will add supply that is not needed at this time, the LHWP does not meet the standard of social equity described in this directive, and fundamentally contradicts the terms of OP 4.07. It will likely reduce the incentive to force the biggest users to practice water-conservation and will not encourage better allocation of resources -- in fact, more likely Phase 1B will have the opposite effect.

5.6 OD 4.15 Poverty Reduction. Para. 28 states: "The Bank's role in supporting poverty reduction through individual investment operations goes beyond financing. The Bank supports sustainable; high return projects and project components that benefit the poor and that would not be done, or would be done differently, without the Bank. Since an improved policy framework can increase the returns to individual projects, Bank project support should also encourage the authorities to eliminate policy and institutional biases against the poor." Moreover, Para. 39. states: "Popular Participation and NGOs Effective implementation and operation of most poverty-reduction projects require the active involvement of the beneficiaries. Active beneficiary participation also should be built into earlier stages of the project cycle. Participation is most critical to the success of projects designed to help specific groups of people. It is important, for example, in family planning, community health, food security, urban upgrading, nutrition, and community water supply projects."

5.6.1 In contradiction of the terms of OD 5.16, this project will create undue burdens on low-income people, not only on project-affected people in Lesotho, but in Gauteng Province, where as noted, water rates have already risen dramatically due to the LHWP and are expected to rise further as the LHWP bills begin to rise. Bank staff have in fact helped to undermine attempts to serve the needs of low-income people and rather than eliminating, are encouraging "policy and institutional biases against the poor." To undertake such a costly infrastructure project well before it is needed shows, we believe, a bias against low-income people (in favour of those associated with-the very profitable construction of the LHWP), who would be better served by changes in water allocation, repair of leaky infrastructure, a daily lifeline amount of water (50-60 liters per capita per day is the Reconstruction and Development Program medium-term objective) and other approaches.

5.6.2 As noted above, affected people have not been fully consulted, not at early stages nor more recently, about the impact of the water pricing implications of the LHWP on poverty. Within the past six months, hundreds of thousands of low-income South Africans have had their personal water supplies cut off as municipal authorities have had to come to grips with persistently lower Intergovernmental Grants (in 1997-98, 85% below the real 1991-92 levels, according to the Financial and Fiscal Commission). These diminished transfers, which explicitly harm low-income consumers, are apparently required because of the ambitious deficit reduction targets in the Growth, Employment and Redistribution strategy adopted in June 1996, following extensive World Bank staff inputs and Bank modelling, but without an adequate safety net for those in default on municipal water accounts.

6. Conclusion

6.1 Summary information. We state the above concerns as summary information. There is a great deal of backup documentation available to justify all of our concerns, including detailed e-mail discussions with World Bank staff that record the Bank's failure to adequately carry out conservation and equity measures, and Bank acknowledgement that a long delay in the next phase of the project is not unreasonable. The claimants will provide the panel with this information, much of which needs to be kept confidential to protect claimants' identity, in a supplemental package.

6.2 Wide support for demand-side management approach. There is, in fact, little controversy over the need for South Africa to focus more on demand-side management. The case for a delay in the LHWP's expansion is strongly supported in South Africa, and indeed the environmental reporter for Business Day newspaper recently (on 19 March) concluded that "calls for delay [in Phase 1B] ... may be justified in order to allow SA to clean up its own backyard concerning water wastage." As the Bank's LHWP task manager himself expressed the shortcomings of previous Bank studies (in an October 1997 memo), "All of this shows that if demand management had been on the table in 1986 at the time of the treaty negotiation, and if the commitment to 1B had not been made on the terms that it was -- then the whole story would be different. Lesson: push the demand management stuff."

6.3 Conclusion. It is therefore logical both for the Bank Inspection Panel to Initiate an investigation, and for the Executive Directors of the Bank to delay any funding approval until a clearer picture emerges of whether the Lesotho Highlands Water Project should go ahead as is currently envisaged, or whether viable alternatives should not, perhaps, first be given a chance. Please contact us at your earliest convenience to record receipt of this request, and to inform us of any follow-up steps that we can take to facilitate your investigation.