A Study to Revisit the LGU Financing Framework and Its Implementation

Final Report

Prepared by:

Anthony J. Pellegrini

and

Ma. Cecilia G. Soriano

for

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FINAL REPORT

A STUDY TO REVISIT THE LGU FINANCING FRAMEWORK AND ITS IMPLEMENTATION

The purpose of this study is to review the implementation of the *Local Government Unit* (*LGU) Financing Framework* since its adoption and presentation to the Consultative Group Meeting for the Philippines held in December 1996 and to propose revisions to the framework. It revisits particular issues of concern such as cost sharing arrangements between the national and local governments and the roles and responsibilities of the Municipal Development Fund Office (MDFO) and the government financial institutions (GFIs). It also looks at the roles and responsibilities of national government line agencies vis-à-vis local government units and provides suggestions for improving institutional arrangements to further enhance local governance and development. Finally, it provides guidance towards harmonization of lending policies and financial incentives to LGUs from various government entities including GFIs.

According to the Terms of Reference, "This study is an initial assessment of the current framework and its implementation. Issues and recommendations emanating from this phase will be pursued through further studies in the future."

This report is comprised of four papers:

I. Assessment of the LGU Financing Framework and its Implementation;
II. Inventory of Financing and Technical Assistance Provided to LGUs from Official Development Assistance (ODA) Sources;
III. An International Perspective on Financing Local Governmental Projects; and
IV. Recommendations on the Strategic Roles and Development of the MDFO.

The last section presents a summary of the main recommendations to implement the Framework.

I. ASSESSMENT OF THE LGU FINANCING FRAMEWORK AND ITS IMPLEMENTATION

The consultants are to "document and assess the implementation of the framework and identify issues to be addressed in the future (short and medium term)."

The *LGU Financing Framework* was formulated by the Department of Finance (DOF) in response to the 1991 Local Government Code (LGC) which mandated the devolution to LGUs of many functions previously carried out by national government line agencies. Although the LGUs were given an increased share of national government revenues and they were clamoring for more direct access to ODA, these would not be enough to meet their increased need for financing. LGUs would have to improve their capacity to generate their own revenues and also gain access to private capital markets. The framework proposed various means through which the GFIs and Municipal Development Fund (MDF) could utilize financial and technical assistance from ODA sources and internally generated funds to help LGUs meet these objectives.

The *LGU Financing Framework* was based on the premise that LGUs have varying degrees of creditworthiness and that LGU credit needs could best be served by a policy of market segmentation, along with a policy of "graduation" of creditworthy LGUs to the private sector. Under this policy, the higher-income, more creditworthy LGUs would avail of private commercial finance except possibly for environmental and social projects; the GFIs would serve the middle tier of LGUs; and the MDF would serve the lower tiers. LGUs were expected to move up the ladder over time. Annex I-A presents the credit policy framework for LGUs in more detail.

The *LGU Financing Framework* also recommended that steps be taken to achieve seven forward-looking reform objectives, namely:

1. Increase LGU use of BOT (build-operate-transfer) arrangements;
2. Develop the LGU bond market;
3. Promote LGU access to private banks;
4. Optimize the involvement of GFIs in LGU financing;
5. Restructure and reorient the MDF;
6. Improve the capacity of LGUs to raise their own revenues; and
7. Tap ODA technical assistance and financing.

While many things have changed since the framework was adopted, the objectives and the basic strategy remain valid. Perhaps the most important developments have been the rapid increase in direct lending to LGUs by the GFIs and the strong credit record that has been built up by the LGUs.

Also significant are the start of an LGU bond market stimulated by the creation of the Local Government Unit Guarantee Corporation (LGUGC) and the reorganization of the MDF into the Municipal Development Fund Office (MDFO.)

A. PROGRESS IN ACHIEVING OBJECTIVES OF FINANCING FRAMEWORK

Progress in achieving the seven objectives of the framework are briefly outlined below, along with issues and concerns raised by various stakeholders such as national government line agencies, local government units, and financial institutions. Consultants' recommendations are given to address each of these.

1. Increase LGU Use of BOT Arrangements

Background

Build-operate-transfer or BOT schemes are mechanisms for bringing private finance and private management to the operation of infrastructure and other public facilities. They can be an effective means for improving the efficiency of service delivery. They can also reduce the potential debt burden of governments, since the entity that is responsible for the BOT scheme would normally be responsible for finance of investments. Depending on the revenue base of the scheme and the structure of the contract, there may or may not be liabilities on the part of the government.

Some progress is being made in the involvement of the private sector in LGU infrastructure investments. Apart from the Metro Manila water concessions however, most of the examples to date are not true BOT or concession schemes. Rather, they are predominantly management contracts.

The *LGU Urban Water Supply and Sanitation Project* financed by the World Bank is the largest program fostering private sector involvement in LGU service delivery. As a condition of eligibility, the LGU must engage a private sector operator in the management of the water utility supported under the project. To date, about 12 LGUs have water systems with private operators. There is a large pipeline of additional LGUs where feasibility studies are at various stages of completion. Under this project, the Development Bank of the Philippines (DBP) on-lends the proceeds of the World Bank loan to participating LGUs while retaining credit risk. The program is targeted at lower tier LGUs. DBP evaluates sub-projects and the creditworthiness of the sponsoring LGU, makes a credit decision and bears full credit risk.

Several other programs have been established which are aimed at supporting private sector involvement in LGU infrastructure through BOT type schemes, but have not yet taken off on a significant scale.

- The ADB has financed an innovative *LGU Private Infrastructure Project Development Facility*. The facility supports the preparation of feasibility studies for LGU projects involving private sector participation. Under the facility, the Land Bank of the Philippines (LBP) makes loans to interested LGUs for project preparation. If a project results, the loan is built into the financing for the project, and becomes the responsibility of the sponsor. Otherwise, the LGU repays the loan to the Land Bank.
- JICA has also financed an interesting *Environmental Infrastructure Support Project*, which supports private participants in LGU infrastructure investments. Sub-loans are made to qualifying private entities for municipal environmental infrastructure. This project is channeled through the DBP.
- The Coordinating Council for Private Sector Participation (CCPSP) is playing an active role through the publication of guidelines and information documents, and the promotion of projects. It is sponsoring an interesting BOT program to bring in private investment and management to *LGU Information Technology*. Under this program, the IT facilities are bid out to private investors for finance, implementation and management under contract over a period of three or four years. The expectation is that the private company can recover its costs by sharing in increased LGU revenues generated by better computerization of billing and collection. No systems have yet been set up under this scheme but apparently it has generated interest on the part of investors. This is a potentially important scheme that needs to be coordinated with the Bureau of Local Government Finance (BLGF) of the DOF. The BLGF has its own scheme that is aimed

at installing systems permitting uniform computerized accounts by local governments. There could be useful synergies if these programs are coordinated.

Among the other types of projects that lend themselves to BOT type schemes are bus, ferry, and port terminals, public markets, industrial estates and high traffic urban road and bridge facilities In addition, solid waste collection and disposal is a high priority sector that lends itself to the involvement of the private sector, but to date there has been little progress in solid waste despite some attempts.

Issues and Concerns

The main examples of BOT type projects at the LGU level that have been implemented to date (e.g. through the *LGU Urban Water Supply and Sanitation Project*), have been cases where the LGU retains ownership of the assets and the private sector operates the assets under a management contract. This is an important reform in improving management of water supply assets and is necessary to build the confidence of the private sector in the water sector. It is therefore a first step toward the objective of the financing framework of expanding the use of BOT schemes as a means of reducing the financing burden of LGUs. This financing objective is not yet being achieved, because the LGUs themselves are borrowing the funds to build or rehabilitate the assets. Achievement of the goal of reducing the public finance burden by the use of BOT type schemes requires the future step of having the private sector involved in financing of the assets.

The experience of the *LGU Urban Water Supply and Sanitation Project,* the JICA-supported environment project and the ADB-supported project development facility seems to indicate that it will be some time before private financing of infrastructure begins to play a significant role in reducing the LGU financing burden. Private sector entities are concerned about political risks inherent in long-term contracts with LGUs.

Many local governments are undertaking revenue-generating projects on their own either because this is seen as a mechanism for increasing their own revenues, because the projects are not felt to be of interest to private operators, or because of lack of knowledge about the mechanisms of BOTs. Some revenue-earning projects, such as markets, bus terminals or industrial estates, that are publicly managed may do better as BOTs. Through a BOT arrangement, the local government should be able to receive fees and taxes that provide additional revenues, while avoiding debt and management risks. However, the potential advantages of BOT arrangements may not always be seen by LGUs to outweigh the perceived disadvantages.

At the national level, implementation of the BOT law has been important in several sectors, most notably power, but there have been difficulties in contracting. Access by concessionaires to national government guarantees has led to large and un-funded contingent liabilities. There are also examples of questionable projects arising from unsolicited proposals and a lack of competition. The lack of a regulatory framework, the lack of transparent approaches for setting tariffs, and the inexperience of LGU officials in dealing with BOTs are key factors leading to uncertainties for investors. To protect against these uncertainties, operators are led to ask for national government guarantees, which the national government appropriately is reluctant to give. The moral hazard of a guarantee by one level of government to protect against actions of another level of government is generally to be avoided.

As LGUs consider BOT and concession schemes which can have great benefits for the local population, they will have to do so with considerable care and with the help of experienced professionals especially in the area of contracting. Regulatory and tariff setting issues also have to be resolved to ensure that risks and rewards are properly balanced among the parties.

BOT schemes offer a valuable opportunity for LGUs to simplify their management burden, better allocate some of the risks of project construction and management, and alleviate somewhat the financing burden for needed services and facilities. However, the adoption of BOTs by LGUs will be slow and gradual over a long period of time. Time is needed to develop systems and procedures to alleviate political risk, resolve regulatory and risk sharing issues, and address concerns over the financial capacity of LGUs to comply with any financial obligations that they may have as part of a contract.

Recommendations:

- The CCPSP, together with NEDA, DILG-LGA, DOF-BLGF, MDFO, and the GFIs, should hold consultation meetings regularly with LGU representatives to review actual experiences with BOT projects and identify measures that need to be taken to make BOT arrangements an attractive financing alternative for LGUs as well as viable propositions for private sector operators.
- A sustained marketing or advocacy campaign can be undertaken to help LGUs fully understand the advantages and disadvantages of BOT and other similar schemes.
- As part of lending policy, prior to making a public sector loan for a revenue-earning project, the GFIs and MDFO should encourage LGUs to consider whether a BOT arrangement would be a feasible alternative to a public sector project. Continuous training by the CCPSP, LGA, and consultants in options, structuring of contracts, and how to analyze tradeoffs is very important.
- Regulatory issues and policies for national government guarantees need to be clarified in order to reduce uncertainties for investors and better balance risks among parties.

2. Develop the LGU Bond Market

Background

Some early progress has been made in the development of an LGU bond market. Bond markets are an important element of a developed financing framework because bond markets are efficient mechanisms for mobilizing resources from a variety of private and semi-private financial institutions, including insurance companies, pension funds, mutual funds, companies and wealthy individuals. For larger sized debt packages, a bond flotation would normally result in lower costs to borrowers than a bank loan. In the Philippines, because private investors have limited knowledge of LGUs as borrowers, and because the domestic bond market is not well developed, this may not yet be the case.

The most relevant development to the facilitation of LGU bond flotations has been the creation of the Local Government Unit Guarantee Corporation (LGUGC). The LGUGC was incorporated on March 2, 1998 to guarantee debt issues of sub-sovereign government entities when these debt issues are financed from private sources. It operates as a private sector corporation supported by the Bankers Association of the Philippines (BAP), and the Development Bank of the Philippines. Its capital shares are owned 49 percent by DBP and 51 percent by some 21 financial institutions. It is the first privately managed local government guarantee corporation set up in a developing country of Asia. Since the start of LGUGC's operations, eight LGU bonds have been floated, all with the backing of LGUGC. Annex I-B presents the features and purpose of these eight bonds. Prior to the creation of the LGUGC, only four LGU bonds had been floated. One was floated by the province of Cebu while the three others were housing bonds guaranteed by the Housing Insurance and Guarantee Corporation (HIGC), a government-owned institution. The total amount floated to date with the guarantee of the LGUGC is 1,355 million pesos. This is on par with the outstanding portfolio of the DBP but is small compared to the outstanding LGU portfolio of Land Bank. However, a good start has been made, and there are prospects for an increasing role for bond market financing.

Issues and Concerns

Many domestic investors in the Philippines are still unfamiliar with existing LGU securities and are wary of the LGU market. Among the factors mentioned by investors as sources of concern are: lack of reliable information about LGUs, the possibility of political interference in project management or in debt servicing, uncertainty about management capacity at the LGU level, uncertainty about the quality of feasibility studies, lack of an independent rating agency, lack of a market for secondary trading, and lack of access to IRA as security for LGU obligations.

A number of steps have been initiated by BLGF to increase the availability and reliability of data about LGUs. The steps underway by BLGF include changing the system of accounts from a cash basis to an accrual basis, and computerization of accounts. The development of a comprehensive LGU information system to include consistent data formats across all LGUs covering finances; outstanding debt and future debt service, budgets, procurement, and a few simple indicators of performance is the next step. This would greatly increase transparency and confidence in local government management as well as help potential investors to assess risks of individual LGUs. BLGF and COA have a large task ahead of them in insuring the proper implementation of these systems and in ensuring and accuracy and timeliness of information. Funds are available under LOGOFIND for this purpose.

A private credit rating agency would be the best way to obtain an indication of the risks of an individual LGU bond. Rating agencies would also continuously monitor LGUs that have bond issues outstanding to provide advance warning to bond holders if the financial condition of issuing local governments was changing in a way that would affect ability to pay debt service. Currently, there are no systematic private ratings of LGUs or LGU obligations because of the low volume of transactions and the lack of economies of scale that would make private ratings a profitable business. The LGUGC, by necessity, performs its own rating analysis prior to making a decision to insure a proposed LGU bond. But issuing credit ratings is not the primary business of the LGUGC and it would be preferable for the rating and guarantee functions were completely separate. The LGUGC has consistently indicated its interest in helping establish an independent privately-owned credit rating agency.

The existence of a trading facility for fixed term bonds would also help increase demand for long term LGU bonds. Some investors, who otherwise would only be interested in a short-term bond, may be willing to buy a long-term infrastructure bond if they had the assurance that they could sell the bond before maturity in case of need or in case financial conditions change. At the moment, there is not much of a fixed term bond market and little in the way of bond trading. The BAP is considering steps to develop a market for the trading of fixed income securities. Such a market could be an important vehicle for capital market development and for increasing domestic savings. Since most commercial debt in the Philippines is comprised of short term or variable rate instruments, there are at present few long or medium term fixed income assets that would be available at the start of the fixed income exchange. The LGU bonds floated to date have maturities of up to seven years, and could be an interesting asset type with which to begin the process of deepening the capital markets. The LGU portfolios of the GFIs could also form the basis for a sizeable pool of tradable fixed income debt if securitized. So far, the GFIs which have looked at securitization have concluded that they did not see any particular benefit to them of doing this. This could change with more competition for LGU business and the existence of the proposed new facility, which would reduce transactions costs and increase the market for such securities.

The GFIs have access to ODA funds as a source of capital for their LGU loans. These ODA funded loans are an alternative to the issuance of bonds by LGUs, and it is important that GFIs do not use ODA funds as a means of substituting for what otherwise would be a domestic bond flotation or securitization.

To date, there are only a few programs where ODA funds are employed to leverage private funding. The JBIC Environmental Infrastructure Support program is one. USAID has supported LGU bond issues through a co-guaranty facility that it has established with the LGUGC. The ADB also has under consideration various schemes that would facilitate private financing of LGUs. The DOF should encourage all donors to use their funds not only for direct, pass-through lending, but also in more innovative ways that would help develop sustainable financing by bringing in domestic private capital. Multilateral and bilateral funding should be seen as an opportunity to develop the domestic credit markets as well as a means of funding projects. The involvement of the multilateral institutions would be particularly useful because their involvement may provide some comfort to domestic private institutions, which might be more willing to participate in schemes if multilateral institutions sponsored those schemes.

Bond issuance is only feasible for large local governments where the size of the bond is large enough to offset the fixed costs of issuing bonds. Small municipalities typically cannot benefit from the lower interest rates generally available from bond floatation and have to rely on bank loans. Recently many countries have established intermediaries, which pool the needs of a number of local governments and borrow on their behalf. At some point in the future, the Philippine LGU bond market would benefit from such an institution.

In a mature LGU financing framework, bond issues should play a prominent role. Bonds bring in a wide variety of investors and offer the opportunity of lower interest rates to LGU issuers than would typically be available through a bank loan.

Recommendations:

- The shareholders of LGUGC should consider an increase in capitalization of the LGUGC to allow it to continue to serve its LGU clients beyond its current capitalization limit. Private rather than public investment is needed. There could be a role for assistance by IFC, JBIC, or the private sector arm of ADB. This should be actively supported by DOF.

- The experience of the LGUs that have floated bonds should be documented and evaluated so that any problems encountered can be addressed immediately and positive experiences made known to more LGUs who may then wish to consider bond flotations as an alternative financing strategy.

- The BLGF, in coordination with the Department of Budget and Management (DBM) and the Commission on Audit (COA), should give priority to the development of systems for the timely publication of consistent information across LGUs on finances, budgets, outstanding debt and projected debt service obligations, as well as a few performance indicators that would facilitate benchmarking comparisons. The objective should be to eventually have all information available publicly, perhaps on the Internet, on a real time basis. This may also have the beneficial effect of improving transparency of LGU management decisions. It would also reduce transaction costs for a potential future private rating agency that could make use of this information to make judgments about the relative risks of LGU issuers. This “information platform” might increase the ability of a private credit rating agency to develop a business in LGU ratings. Because of the complexity of the task, BLGF should consider appointing a full time professional program manager to this job. This can be done within the context of the planned “re-engineering” of the BLGF.

- In the absence of a private rating agency, it is recommended that the BLGF publish a special annual report (perhaps updated semi-annually) on the financial condition of local governments that have already issued bonds, on the repayment experience to date, and on any changes that would affect the ability of the LGU to service its debt. This would not only provide information to existing investors, but more importantly, would serve to inform investors who are not familiar with LGU securities about the performance of these securities. It would also be an ingredient in the development of secondary trading, since potential buyers of listed bonds, would need up-to–date information on the riskiness of these bonds during the period of their remaining life. Consideration should be given to inviting the Bankers Association of the Philippines to help draft the TOR and to help select a reputed local accounting or consulting firm to prepare the first annual report.

- The GFI policy of lending to LGUs at market terms should be firmly adhered to in order to avoid discouraging private funding through bond issues.

- ODA sources should be encouraged to employ lending modalities that utilize ODA funds to leverage private sector funding to LGUs, where this is feasible, rather than focus only on direct on-lending.

- The DOF should consider the feasibility of establishing an LGU bond pooling mechanism. This is one possible future function of the MDFO.

- The DOF and BSP should work with the BAP to identify the rules and regulatory changes that would be needed to support the establishment of a fixed income trading facility that could be used for the trading of LGU securities.

3. Promote LGU Access to Private Banks

Background

A central tenet of the *LGU Financing Framework* is the idea that better off LGUs should graduate from financing by GFIs to financing by private sources including private banks. While there has been some progress in the development of the private bond market, there has been no progress in lending to LGUs by private banks. Some private banks have been purchasers of LGU bonds, but there has been negligible direct lending. Private banks do not have a depository relationship with LGUs and therefore do not have the opportunity of becoming familiar with the management and finances of the LGU in a way that it would if it had a depository relationship. There is also very little knowledge among private banks about the positive experience with the LGU loan portfolio held by the GFIs. The lack of familiarity with LGU lending, the information gaps, and the concerns about political risks were already noted above.

Issues and Concerns

The *LGU Financing Framework* recognized the difficulties of attracting private banks into the LGU market and noted that there are two market-based mechanisms for reducing risk and encouraging private bank lending that need to be undertaken:

- The liberalization of the LGU depository bank regulations, and
- The extension of the IRA intercept mechanism to include private banks

Both of these measures would provide comfort against the political risk faced by private banks in lending to LGUs.

There has been no movement on these measures since the *Framework* was established. The Central Bank and the Commission on Audit (COA) have jurisdiction. The Central Bank and COA have not sanctioned any private bank (except the Philippine National Bank which is a former GFI) to be a depository bank for LGUs. Private banks have indicated that their inability to become a depository bank for LGUs is the chief structural impediment to their entry into the market. There is widespread support for change among private financial institutions and there is a bill pending in congress that would allow private banks to become LGU depositories.

Two reasons have been put forward as to why private banks have not been given access. The first is that the difference between interest earned on the LGU assets by the banks and the interest paid to LGUs would be lost to the "government." The feeling is that because there are very substantial amounts of funds owned by the LGUs, government should not lose the banking profits earned on these funds. However, this argument is contrary to government's privatization policy. It is no different from the argument that the government should be the owner of all public services so that it can profit from managing that service. The opportunity to make profits from an activity is not a good justification for government operation and monopoly in any sector. Banking is a competitive business like others and the more that government can rely on private management rather than public management, the more the public will benefit from the efficiencies of competition and use of assets. LGUs, like citizens, should be allowed to benefit from the better services that can be expected if there was competition for their business. The second reason given is that failure by a bank that held an LGU's deposits would be catastrophic to the LGU and to its citizens. To protect against the consequences of bank failure, a prudent approach would be to pre-qualify a limited number, say three initially, of the best performing and strongest private banks to alleviate any concern about bank failure. Banks should also be held to normal exposure limits to any one LGU borrower and to the LGU sector as a whole.

Private banks will, at least initially, focus on the more creditworthy LGUs. They may also initially favor revenue-earning projects. Many projects that require tenors of 8 to 15 years may be difficult if not impossible to finance under commercial terms so that private bank loans are therefore likely to be limited to special cases. The likely focus of private banks on low risk borrowers is consistent with the "graduation policy' that is the cornerstone of the *LGU Financing Framework.* It is also to be expected that the movement of private banks to the LGU credit market will be gradual even for the best quality loans, as track records are built up. There will have to be a period of confidence building.

In some countries, institutions that rediscount loans made by private financial institutions facilitate private bank lending to local governments. In Columbia, for example, FINDETER (see Section Three below) rediscounts 85 percent of the value of a qualifying loan made by commercial banks to local governments. The establishment of a rediscounting facility is one of the options that could be considered in the Philippines. This is one of the possible roles that the MDFO could play in the future.

An important reason for encouraging private bank lending to LGUs is that currently a high percentage of GFI lending and all of MDFO's lending come from ODA sources. These are for the most part foreign currency loans that bear foreign currency risks. LGU revenues are in domestic currency. The investment needs of LGUs are so great that it is important that domestic currency sources begin to play a larger role in LGU financing.

Other factors are also important and need to be considered in taking steps to encourage private banks to consider lending to LGUs. They include the following:

- Private banks will want to be assured about the quality of feasibility studies, and will be more comfortable when projects are seen to be part of a well-supported local development strategy. This means that project development funds that allow LGUs to hire qualified consultants to develop feasibility studies are very important. Such funds are available under the LOGOFIND project and others. In addition, City Development Strategies that have been conducted in several cities have proven to be a highly successful method of developing an overall set of priorities for a local government. The fact that this approach involves the participation of a broad set of community and private sector participants in preparing the strategy adds to its credibility.

- Private banks are concerned about the political risks of local government lending. They are concerned about the possibility that a new mayor will come to power and for purely political reasons, renounce the projects and/or debt of a predecessor. The decentralization process in the Philippines is still relatively new, dating from the 1991 LGC. Overcoming these concerns will require time for experience to accumulate. Independent rating agencies could help give comfort to banks about the risks of particular LGUs, since rating agencies would cover political as well as economic risks. Also the possibility exists for the LGUGC to insure private bank loans as well as bond issues. LGUGC may find it worthwhile to consider the possibility of working with a private bank to cover an LGU loan. This could be useful in the early stages to introduce a private bank to enter the market on a risk-sharing basis with the LGUGC. LGUGC private guarantees could be a useful (if limited) part of the overall framework for private bank lending to LGUs in the future, which can be called upon in particular circumstances.

- Private banks are not well informed about the financial condition of LGUs. As noted above, an opportunity exists for BLGF to play a very important role in improving the information that is publicly available on local government finances. Some countries are going as far as publishing all information about procurement opportunities, short listing and awards on the Internet. The BLGF program to improve LGU accounting information should be given priority within DOF. A special committee should be established that would monitor the timetable and progress in achieving objectives across all LGUs.

- Private banks are not well informed about the actual experience of LGU borrowing. This experience has been very positive since the enactment of the 1991 LGC and LGU loans have been the best performing sector of the GFI portfolio. A DOF-sponsored information program could be useful in advancing private banks' interest in LGU lending. It could help to establish a dialogue between the DOF and private banks on the credit risks and issues related to LGU loans. As noted above, a helpful measure would be for the BLGF to publish an analysis of the experience with LGU debt on an annual basis, covering bond issues as well as bank loans. This report should be made available to the public and distributed to all private banks and interested investors.

Recommendations:

- The DOF should initiate discussions with COA and BSP to allow selected private banks to become accredited as depository banks for LGUs. It would be prudent to limit the accreditation initially to only a small number of the strongest private banks. Simple criteria should be established for accreditation. For example, only banks with large capital base, acceptable capital adequacy and liquidity ratios, low NPL ratios, and with a wide network of offices throughout the country should be accredited. Also banks should be held to prudent exposure limits to any one LGU borrower and to the LGU sector as a whole.

- The DOF and MDFO should coordinate with NEDA and DILG on ways to increase access by LGUs to funds for local economic development planning and strategy studies and also for project feasibility studies.

- The LGUGC could enter into discussions with private banks to determine whether there is a market for an LGUGC guarantee tied to a private bank loan to an LGU.

- The BLGF, in coordination with DBM and COA, should give priority to the program of developing modern LGU information and accounting system, including a monitoring system for their outstanding loans.

4. Optimize the Involvement of GFIs in LGU Financing

Background

Under the LGU Financing Framework, the GFIs and the MDF were to be "… catalysts to bring LGUs to the mainstream of the private capital markets".

As such, the GFIs were encouraged to:

1. Lend to creditworthy LGUs that cannot yet tap private capital, and adopt a built-in graduation scheme to move the more creditworthy LGUs to the private credit markets;
2. Develop co-financing arrangements or project referral schemes with commercial banks; and
3. Provide limited technical assistance to enhance LGU creditworthiness, particularly in the areas of financial and project management.

GFI lending to LGUs has indeed increased sharply in recent years. The LGU portfolio of the Development Bank of the Philippines (DBP) went from about zero in 1997 to 1.7 billion pesos in 2000. The Land Bank of the Philippines (LBP) went from one billion pesos in 1995 to 11.8 billion pesos in 2000. The GFIs have found that the quality of their LGU portfolio is excellent, in large part because of the requirement that the GFI become the LGU depository bank as a condition of lending along with the pledge of the Internal Revenue Allotment (IRA) in case of non-payment. The non-performing loan (NPL) ratio for the LGU portfolio of the GFIs is well below one percent while the NPL ratio for the financial sector as a whole is reported to be over 18 percent. The Philippine National Bank (PNB), which was a GFI until its privatization, is also lending to LGUs. It is also the only private bank eligible to be an LGU depository. PNB's current LGU outstanding loan portfolio amounts to 3.5 billion pesos with no non-performing LGU loans. Of special interest is the fact that for all of the GFIs, the NPL rate for lower tier

LGUs is about the same as for upper tier or higher income LGUs. As a result, the GFIs are not restricting themselves to the middle and upper tier but are also beginning to lend to the lower tier LGUs that had been thought to be the preserve of the MDFO. For example, over the past five years, approximately 54 percent of Land Bank's LGU loans have been to LGUs in the 3rd to 6^{th} classes. Annex I-C presents comparative data for LBP, DBP and MDFO.

The GFIs have developed the institutional capability for appraising LGU projects and assessing credit risks. This is important because the accounting systems, budgeting systems and the legal framework for local governments are different from those of commercial customers. Because the GFIs are channels of ODA funding, they are also beginning to adapt to the environmental and procurement regulations of the multilateral development banks.

Issues and Concerns

LGU loans have now become an important and profitable part of the portfolio of the Land Bank of the Philippines. Land Bank is a channel of ODA and also uses its own resources to lend to LGUs. The Development Bank of the Philippines, which entered this market more recently, also has had a very positive experience with their LGU credits, and is interested in expanded lending. So far, the DBP has maintained a policy decision to exclusively rely on ODA resources for LGU loans, because of the long-term nature of these loans. It is unclear how PNB will operate in the future given the recent changes in its management and ownership.

The positive experience of the GFIs in lending to LGUs is serving to provide a track record that may, if continued, demonstrate to private banks that the LGU market is a relatively secure and profitable one. Some private banks are keeping an eye on the experience of the GFIs, but have maintained the view that the playing field is not level and that they are at a competitive disadvantage vis-à-vis the GFIs because of the depository privilege and the access of GFIs to ODA funds.

While GFI lending has significantly increased, the goal of the *LGU Financing Framework* related to utilizing the GFIs to catalyze private funding of LGUs through a graduation policy has not materialized. The GFIs have not developed co-financing arrangements or referrals with commercial banks for LGU loans, and a "built in graduation scheme" has also not been developed. This is not necessarily the fault of the GFIs, but is partly because the conditions do not yet exist for private bank lending. Under current conditions, co-financing or syndication might be feasible, with the GFI acting as depository for the LGU and a trustee of the private banks involved in the loans. However, the GFIs have the liquidity to handle most proposed LGU projects themselves, and there is little incentive to involve others. A graduation policy cannot be effective until the private banks can have access to the same credit security measures that the GFIs enjoy, especially depository rights, and they begin to actively look for LGU lending opportunities.

Even after private bank lending to LGUs does begin, it may not be practical to assume that the GFIs would voluntarily pass up profitable business by passing clients to the private sector. DOF would have to define precisely how the "built in graduation scheme" would work and establish this as policy that would be incorporated in the GFI operations manuals.

The current system is one in which national government-owned banks, the GFIs, hold almost all of the LGU debt, and the principle security of that debt is the national government's own IRA allocation to the LGUs. This is not healthy in the long run. The system would greatly benefit from more private market participants and a greater diversification of risks.

Recommendations:

The vision and role foreseen in the *LGU Financing Framework* for the GFIs will not materialize until action is taken to stimulate private bank LGU lending. Under current conditions, the GFIs on their own cannot be expected to be "catalysts" for the "graduation policy." To have an effective graduation policy,

- The DOF, through the MDFO and in coordination with the COA and BSP, must take steps to remove bottlenecks to private bank lending to LGUs; and
- The DOF and the GFIs should define the precise operational characteristics of a "built-in graduation scheme" to be adopted by the GFIs as part of their own operation manual for LGU lending. Having a specific timeframe would be highly desirable.

5. Restructure and Reorient the MDF

Presidential Decree No. 1914 created the Municipal Development Fund (MDF) as:

a) A revolving fund which shall be made available to local governments (provinces, cities and municipalities) as loans which shall be treated as trust funds and amortized by local governments out of their general fund sources; and
b) Capitalized and funded by proceeds of foreign loans, assistance or grants, which are to be made available to the local governments for specific purposes, project components and activities as set forth in international agreements with foreign governments and international institutions.

In line with the graduation policy and assignment of roles contained in the *LGU Financing Framework*, the MDF was to:

1. Target its financing to less creditworthy LGUs and to social/environmental projects;
2. Refrain from providing grants and credits to LGUs that are qualified to obtain GFI loans or have viable BOT projects;
3. Link its funding to technical assistance to improve LGU capacity and creditworthiness for graduation to other sources of credit; and
4. Promote more direct access of LGUs to ODA sources.

Since its creation in 1984, most of the subprojects funded by the MDF were in rapidly urbanizing areas such that the LGU borrowers were either already in the first and second income classes or soon got there. This was mostly because the GFIs were not yet ready to lend to even these high-income LGUs. With these LGUs becoming increasingly more creditworthy and GFIs becoming more open to lending to them, the *LGU Financing Framework* mandated the MDF to leave this market to the GFIs and make its financing resources and technical assistance available to the less developed and less creditworthy LGUs and to projects with social and environmental objectives which usually have long gestation periods or lower financial returns. Higher-income LGUs which could obtain GFI loans for revenue-generating projects but not for these other types of projects would still be eligible for MDF funding under guidelines to be developed under each project.

The MDF was also tasked to promote LGUs' more direct access to ODA funding. Many LGUs had expressed the desire to be able to borrow directly from multilateral banks and other development agencies. Since this was not yet possible for various reasons, steps to make the MDF more accessible to the LGUs seemed to be the next best thing. Demand-driven loan facilities which would allow LGUs to go directly to the MDF and choose the sub-project which they want to implement were therefore developed. The first such financing facility was created under the Community Based Resource Management Project (CBRMP) funded by the World Bank. The second was under the Local Government Finance and Development (LOGOFIND) Project, also funded by the World Bank. These projects were designed in consonance with the other mandate for the MDF to target its financing to less creditworthy LGUs or to projects with social/environmental objectives. The two projects also had significant technical assistance components to improve LGU creditworthiness and capacity to prepare and implement projects.

6. Improve the Capacity of LGUs to Raise Own Revenues

Background

The most important revenue source for local governments is the Internal Revenue Allotment (IRA) from the national government. The IRA amounts to approximately 70 percent of total local government revenue. Locally generated revenue for LGUs is derived from real property taxes, fees and other taxes, business taxes and licenses and receipts from economic enterprises. Opportunities exist for local governments to increase revenues from each of these sources.

Some US $16.5 million were provided under the LOGOFIND project for consultancy services, contractual staff, equipment, supplies and training in support of the objective of improving LGU resource mobilization and monitoring. This includes a number of components designed to strengthen local finance capacity and to increase locally generated revenues. The project provides financing for the improvement of Real Property Tax Administration (RPTA) through tax mapping, records conversion and management, tax collection enforcement, and data computerization. Increased collection of business taxes, user fees, local enterprises and taxes and fees from private operators of local concessions were also to be targeted. Training of LGU officials in financial management could also be undertaken.

Issues and Concerns

The high level of dependence of LGUs on IRA is a major source of concern. The percentage of IRA to total revenues has not changed significantly in recent years. The problem with a system in which LGU revenue is heavily dependent on a national allotment is that the accountability of

LGU officials to their constituents for revenue and expenditure decisions is lessened. Local officials can act as if they are spending other people's money, and avoid the hard decisions associated with raising revenues to cover local expenditures and justifying to the public the link between taxes and services.

There is also a danger that the low levels of internally generated resources will impair the development of a true local government credit market. With the IRA remaining such a dominant part of total LGU revenues, financial institutions might make credit decisions based on the reliability of the IRA pledge rather than the underlying credit worthiness of the LGU and the viability of the project being financed. There is already evidence of this mentality beginning to emerge. The large concentration of LGU debt in the two government financial institutions compounds the problem and could undermine the stability of the LGU financing system.

Much work remains in the important task of improving the capacity of LGUs to raise their own revenues. Capacity building is in part a training issue, but it is even more an issue of designing incentives to encourage local officials to become more self-reliant. The current incentives for raising LGU own source revenues are not sufficient. It would be desirable for the government to consider changes in the IRA allocation formula that would increase incentives for local governments to increase the percentage of total revenues that are accounted for by local revenues. Specific guidelines should be established for local governments with respect to desirable targets. These should cover aggregate own source revenue as well as norms for each major component.

Recommendations:

- LGUs should be given greater incentives to increase own source revenues. An adjustment to the IRA allotment formula should be considered that would result in a higher IRA when an LGU demonstrates a relatively high degree of effort in raising its own resources.
- Some LGUs have recently taken steps to increase their own revenues. An incentive scheme to encourage them to sustain these efforts despite sometimes daunting public opposition should be developed.
- The action plan to enhance LGU resource mobilization and performance monitoring that was agreed under the LOGOFIND project should be given renewed priority. It should cover not only traditional sources of revenues such as taxes but also user fees and profits from revenue-generating enterprises such as public markets.
- A review of the provisions of the Local Government Code with respect to local taxation and fiscal matters would also be useful in making sure that all possible sources of local revenues can be tapped by LGUs.

7. Tap ODA Technical Assistance and Financing

The important role of official development assistance in realizing the objectives set forth in the *LGU Financing Framework* was well recognized. Closer coordination between the donors and concerned government agencies including oversight agencies was called for to ensure that loan and grant financing as well as technical assistance intended for LGUs would meet mutual objectives. How ODA funds could be utilized to increase private sector participation in implementing and financing LGU projects was a major challenge raised by the framework.

The framework also identified four new directions for ODA support, namely:

1. Building up the LGUs' infrastructure pipeline by providing technical assistance to finance project feasibility studies;
2. Supporting an LGU capacity building fund to promote LGU institutional development in the areas of resource mobilization, budget administration, development planning, capital budgeting and investment programming, project preparation, contract management and construction supervision;
3. Establishing market-based credit enhancement mechanisms for LGU BOT infrastructure projects; and
4. Providing grants and long-term credits for poorer LGUs and for social/environmental projects through the MDF, GFIs, and other facilities and promoting innovative LGU-implemented projects and/or greater LGU participation in NGA-sponsored projects.

The inventory of financing and technical assistance provided to LGUs from ODA sources presented in Section II shows how the above challenges to ODA providers and beneficiaries have been met over the past five years.

B. OTHER OUTSTANDING ISSUES

1. Statutory Limits on Debt Servicing

Background

Under Presidential Decree (P.D.) No. 752, the Commission on Audit (COA) certified the legal borrowing capacity of LGUs. Based on the audited financial statements of the LGU concerned, the COA computed the legal borrowing capacity as seven percent of the assessed value of all taxable real property as of the end of the immediately preceding year less outstanding loans and other long-term indebtedness. Since the Local Government Code (LGC) of 1991 repealed the relevant provision in P.D. No. 752, COA Circular No. 94-007 discontinued the issuance by COA of Certifications on Legal Borrowing Capacity to LGUs intending to contract loans, credits, and other forms of indebtedness with any government or domestic private banks and other lending institutions.

Section 324 of the LGC of 1991 stipulates as one of the requirements that the budgets of LGUs should comply with, for any fiscal year, that "full provision shall be made for all statutory and contractual obligations of the local government unit concerned: *Provided, however*, that the amount of appropriations for debt servicing shall not exceed twenty percent (20%) of the regular income of the local government unit concerned".

On April 27, 1995, the Policy Governing Board (PGB) of the Municipal Development Fund (MDF) adopted Resolution No. 04-95 to guide the evaluation of sub-loan proposals from LGUs to the MDF. With respect to debt service limitation, the guidelines provided "that in no case shall both the existing and proposed loan amortizations exceed 20% of the current year estimated annual income from regular sources plus IRA for the current year as estimated by the DBM". In Annex A of the resolution, it was further specified that the current year estimated annual income from regular sources "shall be based on the average annual growth rate of the LGU's income from the regular sources actually realized for the past 5 to 7 years excluding IRA; in no case, however, shall the average annual growth rate to be used for estimating the current year annual regular income of applying LGUs exceed 15%." At present, the Bureau of Local Government Finance (BLGF) under the Department of Finance prepares certifications on debt service limitation, upon request, in accordance with these guidelines.

Issues and Concerns

1) It appears from the foregoing that LGUs intending to borrow from the MDF have to prepare estimates of current income that may not necessarily be the same as those contained in their duly approved budgets for the current year. LGUs may not necessarily have used the average growth rate for the past 5 to 7 years in estimating income for the current year. Depending on individual circumstances, the growth rate could be zero, or an average of the past three years, or even negative. In certain instances, a growth rate exceeding 15 percent could also have solid basis.

Recommendation:

In view of the above, the duly approved current year budget of the LGU concerned should be used as the starting point of analysis. Income projections and assumptions can be reviewed by the BLGF and those that are found to be overly optimistic adjusted downwards, for the purpose of computing debt service limits. The provisions of Annex A of MDF Resolution No. 04-95 could be used as guidelines by the BLGF.

2) It is also not clear what sources of income are to be considered as regular income aside from the IRA. BLGF Memorandum Circular No. 01-2001 which prescribes new quarterly local treasury and assessment reporting formats has a comprehensive listing of income sources to be submitted as Annex A.2. However, they are not classified into regular and non-regular income.

Recommendation:

More specific guidelines on which of these income sources are to be considered as regular income and under what circumstances they are to be considered as such should be issued by the BLGF to guide LGUs intending to borrow not just from the MDF but other lending institutions as well. It should also be clearly specified that loans are not to be considered as part of regular income. Otherwise, more loans would increase the debt service limit, leaving more room for new loans, rather than less. This had happened before in the computation of the national government's own debt service ratio.

3) Furthermore, the LGUs' regular income may already be fully allocated, even before the new debt is taken on, so that it does not really matter whether the total debt servicing for existing and

proposed loans is less than 20 percent or not. There would still not be enough money for servicing the debt.

Recommendation:

To be really meaningful and useful, the certifications issued by the BLGF should state not only that the servicing of existing and proposed loans does not exceed 20 percent of the LGU's regular income but also that it is not allocated for other purposes, for the current year.

4) One major challenge that needs to be addressed is the provision of Section 324 that the debt service limitation is to be observed in any fiscal year. Since the MDF offers loans with 15 /years maturity and three years grace period, the full impact of the debt-servicing burden will have to be considered over 15 years, especially after the fourth year, and not just during the current year. On the other hand, projecting income over a 15-year period is a very difficult and perhaps ultimately fruitless exercise since assumptions can be made as optimistic or pessimistic as one wishes. In the final analysis, compliance with the debt servicing limitation under Section 324 of the LGC is the responsibility of the LGU concerned. This is made especially clear by its title "Budgetary Requirements" and inclusion in Chapter 3 on Budgeting under Title Five on Local Fiscal Administration rather than in Title Four on Credit Financing, as had been the case in P.D. 752.

Recommendation:

It should be made clear to both LGU borrowers and all lenders to LGUs that the responsibility for ensuring budget allocations for debt servicing lies solely with the LGUs themselves. The lenders would be well advised to put explicit provisions and penalties for this in their loan agreements with the LGUs. The lenders should make sure that they are making the loan based on the creditworthiness of the LGUs concerned.

2. Borrowing Capacity or Loanable Amount

Background

In Resolution No. 04-95, the MDF PGB also approved guidelines for determining the loanable amount for revenue-generating and non-revenue-generating projects. For revenue-generating projects, the loanable amount "shall not exceed 18% of the current year estimated annual regular income, plus IRA for the current year as estimated by the DBM, multiplied by the annuity factor of 12 years at 14% per annum (5.660) or the prevailing annual interest rate". For non-revenue generating projects, the loanable amount "shall not exceed 10% of the current year estimated annual regular income, plus IRA for the current year as estimated by the DBM, multiplied by the annuity factor of 12 years at 14% per annum (5.660) or the prevailing interest rate".

Issues and Concerns

1) While it is accepted that the 18 percent and 10 percent ratios for revenue-generating and non-revenue generating projects, respectively, were put in place to be on the conservative side of the

20 percent allowed by law, it is much less understood as to how and why these particular numbers were chosen and why they had to be different for the two types of projects. The likely explanation for the higher ratio used for revenue-generating projects is because the revenues to be generated from the project will put the LGU in a better position to repay its loan. However, it may be more useful to actually examine the relationship between the project's expected revenues and the debt-servicing schedule for the project loan rather than use a standard ratio. For non-revenue generating projects, the analysis will have to be much more complex since alternative sources of revenue with which to repay the debt will have to be identified.

2) In practice, the 18 percent ratio for revenue-generating projects and the 10 percent for non-revenue generating projects is being applied to 80 percent of the IRA, net of the 20 percent mandated by the LGC to be used for development projects. This needs to be re-examined since LGUs use up almost all of their regular income and IRA for personal services, maintenance and operating expenses, and mandatory allocations and have only the 20 percent development fund as possible sources of funding for development projects, for some of which they may need to borrow. A more realistic and conservative approach would be to look at the 20 percent development fund and see what new projects it can support, rather than the 80 percent balance of regular income which is almost always allocated for other purposes already. There is also the question of whether debt servicing for development projects undertaken now can be included in the 20 percent development fund in later years.

While some LGUs interested in borrowing from the MDF have expressed their observation that the current formulae and ratios are too conservative and unduly limit their borrowing capacity, it could also be argued that the formulae are too liberal and could lead to unserviceable debt burdens for some LGUs.

Recommendation:

Instead of following fixed formulae with constant ratios, borrowing capacity needs to be determined through a close examination of the financial situation of the concerned LGU and the financial requirements and benefits of its proposed project, taking into account the observations made above. The variety and stability of the LGU's sources of revenue and the composition and variability of its expenditures including existing contractual obligations have to be analyzed in order to determine the level of new borrowing that it can safely undertake. This analysis will also identify the various steps that the concerned LGU will have to take to increase its revenues or redirect its expenditures so that the appropriate resources will be made available to undertake the planned project, continue its maintenance and operation and repay back the loan. This procedure is admittedly more cumbersome and time-consuming but it will give both the national government and the LGU concerned the comfort of knowing that the loan amount and conditions attached will enable the LGU to pay back the loan in the future without unduly burdening its future budgets.

3. MDF On-lending Terms

Background

The Policy Governing Board of the MDF determines the terms and conditions for MDF loans to LGUs. MDF-PGB Resolution No. 01-92 laid out the principles to be followed in such determination. With regards to the interest rate, this would "be determined annually to apply to all loan agreements signed in the relevant year. The interest rate prevailing during the signing of the sub-loan agreements would remain fixed for the duration of the loan repayment period. These provisions would give borrowing LGUs greater certainty in their future repayments liabilities than the variable interest rate hitherto in use". Furthermore, "a uniform interest rate would apply for all sub-loan agreements signed in a given year, irrespective of funding source, of borrowing LGU, and of category of investment being financed. This arrangement would: (a) facilitate the objective of fostering real growth in the size (i.e. the net assets) of the Local Loans Account (LLA); (b) simplify the management and administration of the LLA; and (c) promote the objective of selection of well-justified LGU investments (by avoiding bias in investment selection which could be occasioned by differential interest rates)."

Said Resolution further stated that "it is considered that subsidies to LGUs with limited borrowing capacity would better be provided through explicit capital grants (administered through the MDF grant mechanisms) allied with loans at a uniform LLA interest rate rather than being hidden in concessional lending terms". "In the initial year (1992) of LLA operation, the interest rate would be set at 14 percent (14%) per annum. The rate would be increased annually thereafter in increments of 1.5 percent (1.5%) until such time as it reached a reference level of the three month weighted average interest rate (WAIR) on time deposits of 61-90 days, based on Central Bank statistics, plus a margin of 2 percent (2%). Thereafter, it would be adjusted annually in line with this reference level."

With respect to the determination of repayment and grace periods, said Resolution states "the economic or useful life of the investments financed from the LLA loans would determine the maximum repayment periods (including any grace periods) of loans. From the economic standpoint and for equity considerations, future generations should not be burdened, thru taxation, with amortizations for depreciated assets that the earlier generation has incurred and benefited from. The periods over which loans are repaid (to include the grace periods) should therefore be made on a per investment category basis. The MDF-PGB shall issue a schedule showing maximum repayment periods per investment category based on estimated average economic lives". Furthermore, "grace periods would only be allowed where the borrowing LGU is unable immediately to service fully the loan debt. In these circumstances, the grace period would be based on two conditions: (a) cash flow of revenue generating projects; and (b) construction period of infrastructure projects."

Issues and Concerns

1) Having the interest rate fixed over the life of the loan and having uniform interest rates across borrowing LGUs and types of projects has been welcomed by LGUs interested in borrowing from the MDF. However, having the same interest rate for all loans, irrespective of funding

source, has been questioned by some LGUs, particularly with regards to yen loans from the Government of Japan which have very concessional interest rates.

2) Despite the provisions of MDF-PGB Resolution No. 01-92 and fluctuations in Treasury bill rates and other market interest rates over the years, no upward or downward adjustments have ever been made to the 14 percent interest rate stipulated for the year 1992. For the LOGOFIND Project negotiated in late 1998, the loan agreement specified 14 percent as a floor below which the onlending rate could not go. This issue has been repeatedly raised by LGUs, particularly when the lending rates of government financial institutions (GFIs) to LGUs dipped below 14 percent, as they did in 1999. It might be interesting to know what the interest rates would have been if the reference rate specified in the Resolution, the three month WAIR on time deposits of 61-90 days plus a margin of 2 percent, had been followed. The LGUs might find that it was to their overall advantage that the adjustments had not been made, considering that the GFIs' lending rates are not fixed over the life of the loan. In any case, the annual increments specified in said MDF-PGB resolution should be reviewed for possible revision.

3) Greater consistency in the determination of onlending rates by the MDFO and GFIs of ODA-sourced funds would also be highly desirable, especially if they are from the same ODA source. If the graduation policy is to work, the factors used to determine onlending rates, if not the rates themselves, should be as uniform as possible.

4) The most important issue to be addressed is why MDF lending rates are supposed to be market-based. Various reasons have been given in the past: (a) to avoid misallocation of scarce resources that could arise from concessional rates; (b) to instill market discipline and prepare the LGUs for graduation to private sources of capital; and (c) to provide for full cost recovery by the MDF. The application of the above reasons to the particular context of MDF loans to LGUs has to be carefully made and if ascertained to be appropriate, should be clearly explained to LGUs so that they may understand and accept the policy of using market-based interest rates.

Recommendation:

All the reasons cited above for making MDF lending rates market-based appear to be as valid for MDF loans to LGUs as they are for other lending situations. First, if lending rates are concessional, say 6 percent when the market rate is 14 percent, then the hurdle rate for sub-projects to be financed will be much lower, making it possible for subprojects whose return on investment is lower than the real cost of capital to be undertaken, effectively with a national government subsidy. The question is whether such a subsidy should be given by the national government, which also has limited financial resources, for sub-projects with low returns or to other sub-projects that have greater benefits and higher rates of return and are able to pass a higher market-based hurdle rate. Secondly, it is envisioned that more LGUs would eventually be able to access private sources of capital through private bank loans or bond flotations. If the national government provides loans at concessional rates. the LGUs would never want to borrow from anywhere else and would have a difficult time doing so if they are used to interest rates well below market rates.

Thirdly, since MDF loans to LGUs are funded from external borrowings of the national government, and not internally generated funds, the on lending terms should enable the government to recover the full costs of these borrowings. Thus, not only the nominal interest rate of the loans should be considered, but also the exchange rate risk, other fees charged by the lending institution, the cost of providing the MDF services, and the cost of covering loan defaults or delays in payments. In the case of the yen loans from Japan, although the nominal interest rate is highly concessional, the fluctuations in the exchange rate between the Japanese yen and the United States dollar have been quite big and unpredictable over the years, such that the national government has been exposed to large foreign exchange risk in servicing these debts. It should be noted that while efforts are made to recover the full cost of borrowed funds that are on lent to LGUs, most of the loans incurred by MDF with on lending facilities for LGUs also give out grants, either in the form of capital grants or technical assistance grants. This is in line with the MDF policy of providing subsidies to LGUs with limited borrowing capacity through explicit capital grants rather than being hidden in concessional lending terms. Technical assistance grants to build up institutional capacity or improve resource mobilization have also been offered through some MDF-implemented foreign-assisted projects.

Having ascertained, for the reasons given above, that MDF on lending rates should be market-based, the next issue to be resolved is the selection of the most appropriate market-based interest rate. Ignoring for the moment the fact that the MDF is being administered by the DOF for the national government, and keeping in mind that LGUs rely on their Internal Revenue Allotment (IRA) from the national government for around 85 percent of their revenues, it is recommended that market-based interest rate be taken to mean that rate that would fully reflect the appropriate risk that the market perceives it is taking when lending to LGUs. Although the market of lenders to LGUs presently consists only of the MDF and GFIs, both of which are instrumentalities of the national government, the risk they are taking in lending to LGUs actually consists of two parts – one is the riskiness of borrowings of the national government itself and the other is the riskiness of lending to the particular LGU concerned. It is recommended that it be the whole money market's perception of the riskiness of national government borrowings that be used, and this is best exemplified by the Treasury bill rates of longer tenor (180 or 360 days). While Treasury bills are admittedly of far shorter tenor than MDF loans to LGUs, they are the national government debt instruments that are traded most frequently (weekly) and would therefore have the most number of observations within a given period. Adjustments for the difference in maturities could be made by adding a fixed or variable number as a margin. The weekly Treasury bill rates (especially for the 180 and 360-day bills) give a clear indication of how the whole market (including both private and government banks) perceives the creditworthiness of the national government. If, for example, the budget deficit of the national government is wider than expected or bigger than in a previous period, the Treasury bill rate goes up. If, however, the deficit is under control, or surpluses are being achieved, then the Treasury bill rate goes down. As mentioned earlier, and as seen last year, when the release of the IRA to LGUs was delayed or even sought to be reduced because of big national government budget deficits, the creditworthiness of LGUs is still very much intertwined with that of the national government which provides most of the LGUs' income.

In addition to the appropriate Treasury bill rate (180 or 360 days), the market-based interest rate for loans to LGUs should include a margin to reflect the creditworthiness of the LGU concerned.

Ideally, this margin should be variable, with lower rates for more creditworthy LGUs and higher rates for less creditworthy LGUs. On the other hand is the argument that lower-income LGUs should be given concessional rates because of their limited ability to repay loans. In the instances where the LGU and its proposed subproject are eligible for grants, the matching grant would serve to lower the effective cost of the loan. When no grants are available, alternative financing arrangements may have to be considered

Periodic adjustment of the new reference rate would also have to be specified and implemented so that the reference rate carries out its role of reflecting the market's perception of creditworthiness of both the national government and LGUs. Details of the computation of the new reference rate and adjustment mechanism will have to be worked out to keep MDF lending rates truly indexed to the market.

5) With regards to repayment and grace periods, a standard maturity of 15 years and grace period of 3 years has been offered for all types of projects, whether revenue-generating or non-revenue generating. The long repayment period during which interest rate is fixed is one very attractive feature of MDF loans to LGUs. The availment by MDF of official development assistance (ODA) as a source of funds for onlending to LGUs is the primary reason it can grant these long-term loans. When government financial institutions (GFIs) are able to avail of ODA funding sources, they are able to offer similar maturities. When GFIs use their own internal funds, they can go up to only five or seven years. Maturities in the intermediate range, between seven and 15 years, may also be considered by the MDF for projects with shorter economic life so that future generations would not be unduly burdened with repayment of the loan. Recently, the MDF-PGB approved a new policy setting maturity periods for loans to purchase equipment at ten years with no grace period.

Recommendation:

Another look as to whether the MDF should tailor the repayment and grace periods of a loan to the economic life of the project it finances might be warranted for the above reason and to make it possible for the LGU to consider new projects and new loans after it has fully or partially paid off existing loans.

4. Financing Mix for Various Projects

Background

While the LGC devolved to LGUs the responsibility for basic social services such as health and social welfare and for environment-related concerns such as community-based forest management, solid waste management and sewerage, these activities remained on the list of priorities of the national government as part of its commitment to various human and sustainable development initiatives of the United Nations. These projects also had significant externalities and impact on the wider community and LGUs were not completely free to fail in delivering these basic services. The National Economic and Development Authority (NEDA) thus commissioned a study "Developing an Action Plan for the Financing of Local Government Projects with Social and Environmental Objectives" to look into the appropriate level of national government support for health, environment, rural infrastructure, rural water supply and integrated area development projects of LGUs. Together with inputs from concerned national government agencies such as the DOF and local government units, this study formed the basis for guidelines issued by the Investments Coordination Committee (ICC) of the NEDA Board in July 1997 to be applied to ODA-assisted projects for LGUs. The guidelines specified the percentage of project cost that could be given by the national government as capital grants and the types of projects and income classes of LGUs that would be eligible for the grants.

Issues and Concerns

1) There is some inconsistency in the application of the ICC guidelines on subsidies across institutions, across programs and across funding source. In addition to the MDFO, the GFIs also lend to LGUs but the GFIs do not give grants. For example, if MDFO finances a health facility or a slaughterhouse in a 5th and 6th class LGU, the facility would benefit from a subsidy. If a GFI financed the same facility, a subsidy would not be available. Even within the MDFO, subsidies vary depending on the approved loan-grant-equity mix for the project or program being administered. For the LOGOFIND and CBRMP, which are World Bank-assisted projects being implemented by the MDFO itself, the cost sharing schemes are fully consistent with the ICC guidelines. However, several projects which are being administered by the MDFO for other national government line agencies deviate from these guidelines and among each other, even if they are all involving municipal or rural infrastructure. One group of projects are those which were designed and approved after the passage of the Local Government Code but before the adoption of the ICC guidelines. These include the DAR's Agrarian Reform Communities Development Project funded by the World Bank and the DILG's Philippine Regional Municipal Development Project funded by the Asian Development Bank (ADB). Another group of projects was prepared after the approval of the ICC guidelines but have as legal basis the Agriculture and Fisheries Modernization Act (AFMA) that became effective in February 1998. These include the Mindanao Rural Development Project funded by the World Bank and the Infrastructure Project for the Enhancement of Rural Productivity to be funded by the ADB, both projects of the DA. Various rural infrastructure programs implemented by the Estrada administration to secure food security and funded by internally generated budgetary resources also had their own cost sharing schemes.

Recommendation:

A review of the ICC guidelines and ICC-approved financing mix for foreign-assisted projects as well as national government policy on NG-LGU cost sharing for locally funded projects needs to be undertaken to bring about greater consistency in the level of national government support for LGU-implemented projects. Efforts should be made to rationalize the cost-sharing formula currently being applied by all government entities lending to LGUs, including those for devolved activities not included in the initial ICC guidelines. The cost-sharing formula and guidelines to be adopted by the government should be uniformly applied to all projects, whether foreign-assisted or internally-funded.

In carrying out the review, the two basic principles for giving continued national government support for facilities and activities that have already been devolved to LGUs should be reiterated and borne in mind. The first is that the LGU sub-project cannot be expected to achieve full cost recovery under reasonable assumptions. The second is that the LGU sub-project has substantial positive externalities or removes significant negative externalities such that the LGU is not free to fail in the provision of the concerned service or facility.

A distinction may need to be made between general financing facilities that can be approached directly by the LGUs with sub-project proposals and programs being sponsored by national government agencies responsible for a particular sector, such as the DA or DENR, to achieve certain national goals. In the case of the latter, the sponsoring agency reviews and prioritizes LGU sub-project proposals to determine how much they can contribute to the achievement of the stated objectives of the program. The sponsoring agency is in a good position to judge the positive externalities involved. For example, the DA can prioritize farm to market roads according to how much increase in production and productivity can be expected from them, depending on their locations and the types of crops planted in those locations. Those with the greatest contribution to a national goal, such as food security, could merit a bigger matching grant from the national government. Grants for general purpose roads, whose benefits are more widespread and harder to quantify, would be more difficult to justify.

2) There is also the question of the general level of grants. Many of the lower-income LGUs have said that they would like to implement a sub-project but cannot afford to borrow the required loan amount or even put up the required equity out of their current revenues.

Recommendation:

Some LGUs may really need to improve their resource mobilization before they can even afford a small sub-project. Their revenue base may really be too small to support any kind of capital investment. In this case, the bigger capital grant from the national government that the LGU desires is meant to cover the LGU's own resource gap. The most prudent thing is for the national government to assist the concerned LGU in tapping all possible sources of revenue or realigning his expenditures so that there would be some investible funds generated. Thus, capacity building grants or technical assistance to improve resource mobilization or expenditure management would be more appropriate and beneficial in the long run.

3) Another observation is that the larger grants that are given to lower-income LGUs may serve as a disincentive for them to do their best to increase their own revenues. In some projects, high-income LGUs are not eligible for grants even for non-income-generating projects. While equity considerations would justify these bigger grants for poorer LGUs, as would practical consideration of the fact that they would otherwise not be able to afford the desired sub-project, appropriate incentives should also be put in place to make these LGUs strive harder to raise their income levels and the disincentives for higher-income LGUs removed.

Recommendation:

While it is possible to adopt a loan-grant-equity mix that gives the same percentage of grant to all LGUs regardless of income class, on the assumption that higher-income class LGUs would be undertaking bigger projects so they would need as much assistance as lower-income class LGUs, that percentage would probably have to be lower than the percentage presently being given to lower-income LGUs and they may then not be able to afford their desired sub-projects. Limitations or conditionalities for further loans could be put in place as an alternative. For example, an LGU may not be allowed to borrow again until its income class has improved or a certain level of increase in own source revenues has been achieved. Limits on borrowing can also be set as a percentage of its own source revenues. Conditionalities associated with the disbursement of the current loan of the LGU could also be imposed as part of the sub-loan agreement and monitored closely during sub-project implementation.

4) It has also been observed that while blue and green environmental projects are eligible for grants, brown environmental projects are not. The loan-grant-equity mix for community or area upgrading in slums and other depressed areas has also not yet been determined to date.

Recommendation:

Although solid waste management had been devolved to LGUs by the LGC, and were made eligible for LOGOFIND financing, no grants had been provided because it was thought possible for LGUs to draw up and implement full cost recovery plans and because the negative externalities of LGUs failing to deliver this service had been underestimated. The appropriate policy framework for solid waste management that would have guided the determination of those grants had also not yet been drawn up.

In January 2001, within the first week of her presidency, President Gloria Macapagal Arroyo signed Republic Act No. 9003 into law, an act providing for an ecological solid waste management program. While LGUs would still be primarily responsible for the efficient management of solid waste generated within their respective jurisdictions, national government agencies, particularly the Department of Environment and Natural Resources, were mandated to provide technical and other capability building assistance and support to the LGUs. The DENR Secretary was designated as the Chair of the National Solid Waste Management Commission which was mandated to prepare the National Solid Waste Management Framework which would guide the preparation and implementation of local solid waste management plans and projects. While LGUs were given the authority to collect solid waste management fees in amounts sufficient to cover direct costs, fiscal and non-fiscal incentives were also granted, consistent with the provisions of the Omnibus Investments Code or E.O. 226. LGUs whose solid waste management plans have been approved by the Commission were also entitled to receive capacity building grants. A Solid Waste Management Fund to be managed by the Commission was also created, to be sourced from fines and penalties, proceeds from permits and licenses, donations and grants from domestic and foreign sources, and from specific appropriations for the Fund under the annual General Appropriations Act. The Fund may be used to finance products, facilities, technologies and processes to enhance proper solid waste management; awards and incentives, research programs, information activities, technical assistance and capability building activities. With the adverse effects of uncollected garbage on public health, aesthetics and even business investments having been made quite obvious by the breakdown of garbage collection services in many parts of Metropolitan Manila over the past year, and the expectation that the National Solid Waste Management Framework would be prepared within six months after the National Solid Waste Management Status Report is prepared under the leadership of DENR, and the mechanics for the Solid Waste Management Fund worked out soon, the question of

LOGOFIND grants for LGUs implementing solid waste management sub-projects can be revisited. If deemed desirable and affordable by the national government, the appropriate institutional mechanisms and linkages will have to be identified so as to comply with the provisions of both the law and the LOGOFIND loan agreement with the World Bank.

With regards to community or area upgrading, the appropriate loan-grant-equity mix could also be determined if the appropriate policy framework could be developed. Foremost among the questions to be answered is which national government agency shall work with LGUs in addressing the needs of squatter communities or depressed areas.

5) There is also the question of the long-term financial sustainability of the subsidies partly because of a lack of clarity about who is responsible. In principle, subsidies should be carefully targeted, transparent, non-distorting, and financially affordable. The determination of a particular subsidy level should be based not only on the basis of "need" of particular types of programs, but also on the affordability of the subsidy scheme to the government when scaled up. This means making an assessment of the demand for the subsidy on an annual basis and the amount of budgetary and ODA resources available to meet that demand. Fixing a "desirable" level of subsidy in the absence of an analysis of the macro financing implications will lead to inconsistently applied programs that have financing difficulties.

Recommendation:

The respective roles of the line agencies and MDFO in developing subsidy policies for various types of programs should be looked into. Where a line agency has responsibility for certain programs, e.g. schools, clinics etc, the line agencies should develop long-term programs and long term financing plans, which would also be presented to the appropriate oversight agencies for approval. Any subsidies should apply to all similar projects whether funded by donor agencies or internally generated funds.

The oversight agencies particularly the DOF and DBM should also make estimates of how much the national government continues to give as grants to LGUs for devolved activities and how much it can really afford. Consideration of realistic levels of revenues that the national government can really collect and projection of its own debt servicing needs as well as those of government corporations whose liabilities are being transferred to the national government such as the National Power Corporation should be made so that appropriate amounts can be set aside for grants to LGUs. It is only within this budget envelope that sustainable levels of grants can be determined and high expectations avoided.

5. Institutional Arrangements

a. The Changing Roles of National Government Agencies (NGAs) and LGUs

Background

The Local Government Code (LGC) of 1991 introduced a paradigm shift in relations between the national government and local government units by declaring it the policy of the State "that the territorial and political subdivisions of the State shall enjoy genuine and meaningful local autonomy to enable them to attain their fullest development as self-reliant communities and make them more effective partners in the attainment of national goals. Toward this end, the State shall provide for a more responsive and accountable local government structure instituted through a system of decentralization whereby local government units shall be given more powers, authority, responsibilities, and resources. The process of decentralization shall proceed from the national government to the local government units". [Book I, Title One, Chapter 1, Section 2(a)]

To operationalize the principle of decentralization, the national government was to provide funding support and technical assistance to LGUs so that they may carry out their newly devolved duties and responsibilities and participate more actively in national development. In addition to being given "the power to create and broaden their own sources of revenues", they would also have "the right to a just share in national taxes and equitable share in the proceeds of the utilization and development of the national wealth within their respective areas". [Section 3(d)] "The realization of local autonomy shall be facilitated through improved coordination of national government policies and programs and extension of adequate technical and material assistance to less developed and deserving local government units". [Section 3(k)]

Integral to the process of decentralization is enhanced consultation by national agencies with and participation of local government units as well as non-governmental and people's organizations. Likewise declared as a policy of the State is the requirement that "all national agencies and offices (to) conduct periodic consultations with appropriate local government units, non-governmental and people's organizations, and other concerned sectors of the community before any project or program is implemented in their respective jurisdictions". [Section 2 (c)] Furthermore, "the capabilities of local government units, especially the municipalities and barangays, shall be enhanced by providing them with opportunities to participate actively in the implementation of national programs and projects". [Section 3(g)] "National agencies and offices with project implementation functions shall coordinate with one another and with the local government units concerned in the discharge of these functions. They shall ensure the participation of local government units both in the planning and implementation of said national projects". [Chapter 3, Section 25(b)]

Issues and Concerns

While the LGC provided that "national agencies or offices concerned shall devolve to local government units the responsibility for the provision of basic services and facilities enumerated in this Section within six (6) months after the effectivity of this Code" [Chapter 2, Section 17 (e)] and that "regional offices of national agencies or offices whose functions are devolved to local government units as provided herein shall be phased out within one (1) year from the approval of this Code" [Chapter 2, Section 17 (h)], the pace at which national government agencies have reorganized their national and regional offices, refocused their activities and realigned their budgets and priorities in light of the devolution and decentralization mandated by the LGC has been uneven and largely left to the discretion of the head of agency. No incentives have been given and no sanctions imposed on those who have effectively devolved the services and facilities mandated by the LGC and those who have not, respectively.

Two of the more effective means for encouraging the concerned national government agencies to shift their focus from implementing projects and providing services themselves towards more policy direction, standard setting and providing technical assistance to LGUs is through the annual budgeting process and the design and implementation arrangement of foreign-assisted projects. Individually and as the oversight agencies in the Development Budget Coordinating Committee (DBCC) and Investments Coordination Committee (ICC), the Department of Budget and Management (DBM), the National Economic and Development Authority (NEDA), and the Department of Finance (DOF) can play key roles in moving the decentralization process forward. The LGU Financing Policy Framework was formulated to provide funding support for the devolution process primarily from official development assistance. The same principles could be followed even in the allocation of internally generated funds.

Recommendation:

An assessment of how national government agencies have actually devolved to LGUs the responsibilities and powers enumerated in the Code would provide a useful tool for measuring the progress that has been achieved so far and for preparing future work programs. The actual devolution process can be measured in terms of the number of plantilla positions that have been devolved to LGUs or otherwise eliminated, realignment of the agency budget to remove expenditures for activities that have already been devolved, and the design of foreign-assisted and locally-funded projects that involve LGUs. Some donors have initiated steps or shown interest in supporting the conduct of such an assessment. With the tenth anniversary of the Local Government Code coming up on October 10, 2001, a coordinated and cooperative effort involving the national government, LGUs, and their partners in development would be doubly meaningful.

More manifest political will in adhering to the spirit and provisions of the Local Government Code would also move national government agencies to more concretely reflect these in their future organizational structure, budgets and activities. The President could direct all Cabinet members to review their mandates and operations and refocus or realign these where necessary. The Oversight Committee headed by the Executive Secretary with representatives from the Senate, House of Representatives, Cabinet and leagues of local government units could closely monitor the implementation of this directive. Only through a concerted and determined effort on the part of national government officials as well as greater activism on the part of local government units will the vision of participation and development contained in the LGC be brought to fruition.

b. The Community-Based Resource Management Project (CBRMP)

Background

With respect to the environment, the LGC of 1991 states that "local government units shall share with the National Government the responsibility in the management and maintenance of ecological balance within their territorial jurisdiction, subject to the provisions of this Code and national policies". [Chapter 1, Section 3(i)]

In particular, devolved to the municipality or city were " water and soil resource utilization and conservation projects; and enforcement of fishery laws in municipal waters including the conservation of mangroves" and "pursuant to national policies and subject to supervision, control and review of the DENR, implementation of community-based forestry projects which include integrated social forestry programs and similar projects; management and control of communal forests with an area not exceeding fifty (50) square kilometers; establishment of tree parks, greenbelts, and similar forest development projects" as well as "solid waste disposal system or environmental management system and services or facilities related to general hygiene and sanitation". Devolved to the province or city, "pursuant to national policies and subject to supervision, control and review of the DENR", were "enforcement of forestry laws limited to community-based forestry projects, pollution control law, small-scale mining law, and other laws on the protection of the environment". [Chapter 2, Section 17 (b)]

Issues and Concerns

There has been some confusion as to whether CBRMP is an environmental project or a financing project. Corollary to this is the question of which national government agency should be the lead implementing agency for the project, the Department of Environment and Natural Resources (DENR) or the Department of Finance (DOF)? If it is indeed the DOF through the MDF, what then is the role of the DENR and other line agencies such as the Department of Agriculture?

Recommendation:

From the outset, the objective of CBRMP has been to provide LGUs with improved access to official development assistance so that they may undertake community-based forestry projects and other small-scale projects that have been devolved to them by the LGC, as shown above. More direct access to ODA has long been a clamor of LGUs and with the restructuring of the MDFO, LGUs could be provided with financing facilities that they can approach directly for implementing projects of their choice. The World Bank has provided funding support to create such facilities through two projects – the CBRMP and the Local Government Finance and Development (LOGOFIND) Project. In the CBRMP, LGUs can go to the MDFO for financing of small community-based environmental rehabilitation and resource management projects. Under LOGOFIND, the financing facility can be tapped for a wider selection of sub-projects that LGUs can choose from. Both projects are being implemented by the MDFO to provide funding support for LGU sub-projects from ODA sources. Both projects are characterized as demand-driven because LGU sub-projects are not pre-determined during project preparation and design. It is the financing facility itself, to be operated by the MDFO, which is prepared and set up to accept and process LGU proposals for sub-projects.

The paramount importance of technical assistance from the concerned national government agencies to ensure the success of the project is well recognized and the mechanisms to secure such assistance and support now exist at both national and regional offices. The Department of Finance entered into memoranda of agreement with the concerned government agencies at the start of the project in 1998. Efforts to reach common understanding and agreement with the leadership in these agencies during the previous administration resulted in the issuance of joint memorandum circulars. The same efforts may need to be undertaken to obtain the cooperation of the present heads of the national government agencies concerned. Greater clarification of the changing roles of NGAs and LGUs in light of the provisions of the Local Government Code would help to resolve some issues that impede the smooth implementation and future sustainability of LGU sub-projects. Discussions among the concerned NGAs on their respective roles in the CBRMP would also be useful as long as it is clear to everybody concerned that the LGUs are supposed to be in the driver's seat.

II. AN INVENTORY OF FINANCING AND TECHNICAL ASSISTANCE PROVIDED TO LGUs FROM ODA SOURCES

The consultants had been mandated to provide an "…inventory of current financing and technical assistance to LGUs. The inventory will include loans, grants and capability building efforts given to LGUs from ODA sources."

This effort is deemed important in order to provide a database that can be used to promote consistency in the levels of national government support and roles of national government agencies in foreign-assisted projects involving LGUs. The cost-sharing and implementation arrangements for these projects as well as the relending terms to LGUs have been entered into the database for cross comparison and further analysis.

Annex II-A provides a list of 23 lending facilities to LGUs utilizing ODA funds. The lending facilities are classified as to whether they are coursed through the GFIs (LBP or DBP) or through line agencies (DOF-MDFO or other line agencies). Annex II-B provides information on 22 foreign-assisted projects that give grants to LGUs for capital outlays for basic services or infrastructure facilities. They are classified by sector – health, education, agriculture and agrarian reform, water resources, rural development and urban development.

More importantly, the database will serve a practical purpose in better aligning technical assistance and capacity building grants with infrastructure projects or financing facilities. One major constraint that limits the pipeline of LGU projects that can be financed by available funds is the lack of expertise on the part of LGUs to prepare feasibility studies and the lack of funds that LGUs can access to secure such expertise from consultants. On the other hand, there have been many capacity building programs funded mostly by bilateral donors that have succeeded in organizing communities and training LGUs in local development planning and project identification. Some of these have funded or otherwise caused the preparation of feasibility studies for projects which the community and/or LGU would like to undertake. These LGUs could be made much more aware of the various financing facilities available in the MDFO as well as GFIs that could be tapped to finance the capital project itself. Annex II-C provides a list of 48 capacity building and technical assistance programs that are ongoing or have recently been completed. They are also classified by sector – health, agriculture and agrarian reform, natural resources and environment, governance, rural and urban development.

Project fact sheets on each of the individual projects have been compiled and submitted to the MDFO in electronic and hardcopy forms. In addition to information on the project objectives, components and costs, funding source, target areas and implementing agencies, the municipalities and provinces participating in these projects have also been identified and classified by income class, to the extent possible. Details on the cost-sharing arrangement in percentages and million pesos have also been gathered for each of the LGU sub-projects.

III. AN INTERNATIONAL PERSPECTIVE ON FINANCING LOCAL GOVERNMENT PROJECTS

The consultants are asked to "…document the international practices in financing local government projects, and identify the best practices that may be applicable to the Philippine setting."

This section of the consultant's work reviews the North American, European, and Japanese experience as well as the experience in developing countries with financing local government projects. The report gives numerous examples and presents selected examples in Annex III-A.

INTRODUCTION

While there are many similarities, the characteristics of municipal finance systems vary from country to country. The variations arise primarily out of different legal traditions, different institutional frameworks, the level of development of the financial and banking sector, and differences in government policy.

1. Access to private capital via bonds and bank loans

In the US and much of Europe, a sophisticated system has evolved in which municipalities have access to multiple sources of capital competing to serve local government needs. The two principal sources of capital available to local governments in developed economies are bonds and bank loans.

In countries where bond flotation has become a significant business, independent credit rating agencies and private bond insurance companies have played a significant role in market development. Bond markets involve large numbers of diverse investors who need to make informed decisions about whether to buy a bond or not. These investors depend on independent assessments of the credit risks involved in bond issues. In contrast, when a bank is deciding whether to make a loan, the bank can employ its own staff to do the analysis necessary to determine the credit quality of a loan application. However, in the case of bonds, it is not practical for the many financial institutions and individuals who invest in bonds to each do their own analysis of bond issuers. They therefore rely on a rating given by credit rating agencies, and use this information to compare the risks of alternative investments. Both a primary and a secondary market in bonds require publicly available risk assessments of individual bonds.

Independent credit rating agencies are therefore a key institutional requirement for bond market development.

2. The role of private bond insurance

Private bond insurance has developed as an important means of credit enhancement because many investors are willing to pay a premium to receive the assurance that in case of default by the bond issuer they will be paid. Insured bonds have higher credit ratings (approximating the credit rating of the insurer) and therefore issuers of insured bonds enjoy lower interest rates. There is currently about $ 1 trillion of bond insurance in force. The vast majority is for debt issued in the US but the non-US bond insurance is rapidly growing especially in Europe, Japan and Australia. About 50 percent of new municipal issues in the US are enhanced by bond insurance. The percentage of total dollar value of bonds that are issued with bond insurance is significantly less than 50 percent because it is primarily the smaller, less well known municipalities with smaller loans that benefit the most from the enhancement of bond insurance. Bond insurance and bond guarantees refer to essentially the same financial product.

3. Both bonds and bank loans should be available to local governments

In the USA, both bank loans and bonds are common, but municipal bond securities are the most important way that state and local governments borrow money to finance their capital investment and cash flow needs. An unusual feature of the US market is that holders of municipal bonds are exempt from federal tax on interest payments. The favorable tax treatment means that investors will accept lower interest rates for municipal bonds than other bonds, giving these bonds an advantage over bank loans.

In Europe, until recently, bank loans had been the primary vehicle for municipal finance. Bank loans were, in large part, the quasi-monopoly business of specialized, often government-owned, banking institutions that had a special charter to conduct municipal lending. With banking liberalization and privatization in Europe, the privatized financial institutions and remaining government-owned institutions had to compete with other commercial institutions. As competition has been encouraged, margins have decreased, leading to lower interest rates, tenors have been lengthened, and new financial products have evolved to meet particular needs. Today, bond financing is increasingly important in Europe. Innovations including securitizations and project finance and various forms of structured financial products are expanding rapidly.

4. Control of local government indebtedness

The municipal financial system can be important in providing incentives to local governments to improve management performance. For example, access to capital requires municipalities to provide a level of information, and to demonstrate a standard of management and performance, that this itself is an important factor in promoting good government. The desire on the part of local governments to satisfy the requirements of the financial markets to raise capital has often been felt to be as important as laws and regulation in positively influencing good local government behavior. But the incentives built into the financing system can be negative as well as positive when the financial policies are poorly designed. For example, national government guarantees of municipal debt or the understanding that there will be national bailout have allowed local governments to borrow excessively and to default with little in the way of subsequent consequences. This was the case several years ago in Brazil when states exploited their relationship with their own state banks to finance deficits without regard to commercial standards of creditworthiness in anticipation of federal bailouts.

Most governments control the level of sub-national indebtedness with the objective of maintaining macro-economic stability and achieving a sustainable level of debt. This is most often done through limits on the stock of debt e.g. through ratios such as total debt to total annual normal revenue; or limits on the flow of debt through ratios such as debt service to annual revenue. Such systems depend on the timely flow of reliable information and realistic assumptions of revenue forecasts and expenditures. An independent credit rating agency is usually the most objective judge of the realism of such estimates. Bolivia limits the total value of debt to 200 percent of current revenue and limits debt service to 20 percent of current revenue. Poland limits debt service to 15 percent of total revenue. Brazil limits debt service to 15 percent of total revenue or the operating surplus for the previous year, whichever is lower. In Hungary, as an incentive to increase revenue generation, regulations limit borrowing in any year to 70 percent of own generated revenues for the year.

5. Specialization and competition

The policy in most developed economies of encouraging competition among financial institutions for local government business has not led to the elimination of specialized institutions. These institutions still exist in advanced economies and are still being created. In some cases, formerly public institutions such Banco Credito Local of Spain, and Dexia continue after privatization to use their specialized knowledge of local governments to serve a large part of the market. In other cases, publicly owned institutions like the US and Canadian bond banks have remained public and serve specialized needs.

This report concentrates on the characteristics of these specialized entities and provides a fairly large number of examples of the better performing or more interesting institutions because they may offer lessons for the possible evolution of the MDFO in the Philippines. Annex III-A presents a summary table for selected examples of international experience with specialized municipal funds.

A. UNITED STATES EXPERIENCE

1. Municipal Bonds and Bond Banks

In the US, a very large and diversified bond market has developed for financing the needs of local governments. There is currently in excess of $1.5 trillion in outstanding municipal bond debt in the US, consisting in the obligations of approximately 50,000 local government issuers. Individual local governments have direct access to this market and to the private credit ratings and insurance institutions that are part of the system.

The fact that municipal bonds are actively traded has been an important factor in prompting the growth of this market because even investors who may have only a short or medium term horizon can invest in long-term bonds knowing that they can be sold at any time in the secondary market.

Despite the efficiencies of the bond market, many smaller local governments are not able to take advantage of this market on their own because of the relatively high fixed costs of arranging bond finance. These costs include disclosure documentation, bond insurance and the cost of obtaining a credit rating. For large bond issues, the fixed costs represent only a small part of total interest payments. This gives large municipalities with large borrowing needs a cost advantage over small municipalities with small issues.

To solve this problem, approximately 17 state governments in the US have established state chartered “bond banks” which have the objective of taking advantage of economies of scale in bond issuance. Bond banks, for the most part, are institutions that pool the needs of municipalities, and issue bonds in their own name for subsequent re-lending to the municipalities. Typically, bond banks collect the borrowing needs of municipalities over a period of several months and issue two or three bonds during the course of a year to cover these needs. All bond banks establish a reserve fund for added security and often, but not always, also benefit from guarantees by the State government to cover debt service obligations in case of default. The bonds are issued in the name of the bond bank and participating local governments re-pay individual loans to the bond bank so that the bond bank can meet its own obligations. In order to minimize interest rate risks, maturity risks and sometimes currency risks, the terms of loans to participating local governments are carefully matched to the terms of the bond banks own market borrowing. Local governments participating in a given issue provide revenue pledges and sometimes, also general obligation pledges to provide security to the bond bank loans.

Application processes for local government units are streamlined when using a bond bank in comparison to the information and disclosure requirements of a direct issue by a local government. Typically, the application form requests basic information including: the purpose of the loan, total project cost, funding sources and project status. In addition, background information is requested on numbers of employees, tax levy and assessments, collection history, and a schedule of existing debt, and audited financial statements.

In times of falling interest rates, bond banks have issued bonds for the purpose of refinancing past debts at better rates and returning the savings to its participating local government units. Credit ratings of bond bank issues are typically investment grade, even though the majority of local government units that borrow from a bond bank do not themselves have credit ratings. It is likely that if credit analyses were done of the portfolios of U. S. bond banks, the range of loans to municipalities that would themselves qualify as investment grade would vary from 40 to 80 percent of the portfolio of a typical bond bank. By substituting its own higher credit rating for that of the local governments that it serves, bond banks are able to make available lower interest rate loans to many municipalities than they would be able to obtain on their own. Defaults by local governments have been minimal.

Example: Maine Municipal Bond Bank

The State of Maine established the Maine Municipal Bond Bank in 1973. More than 400 local government units in the state of Maine have participated in Maine Bond Bank loans. These are used for school construction, general municipal projects and water and sewer construction. The bank has a reputation for strong professional management and careful collection procedures. For example, the bank continuously monitors the financial position of all of its borrowing local government entities to ensure that they retain the ability to pay their debt service obligations and to give management a warning in case of emerging financial difficulties on the part of a municipality that has outstanding debt to the bond bank. By its charter, the Maine Bond Bank must maintain a reserve fund at least equal to maximum annual debt service on total outstanding bonds. As added protection to bond holders, the state treasurer is authorized to intercept any state funds due to a local government and to divert these funds to the reserve fund in case of deficiency. The state government has also given a "moral obligation" pledge to make up any deficiency in the reserve fund. There has never been a default in payment of bond obligations by the Maine Bond Bank to its bondholders, nor by a participating local government to the bond bank. *Example: Vermont Municipal Bond Bank*

The Vermont Municipal Bond Bank has been in existence for about 30 years. It typically issues debt once per year. It immediately lends the proceeds of its bond floatation to a list of local institutions that have received prior approval by the bank's board of directors. Because Vermont is a relatively small state, its borrowings are in the 40 to 50 million-dollar range.

The Vermont Bond Bank maintains a reserve fund that is at least 1.25 expected annual debt service. The sub-loans in the bank's portfolio are secured by a general obligation pledge from the borrowing entity. Bondholders have additional protection from the legislation creating the bond bank. This legislation included a pledge by the state legislature to appropriate funds if necessary to replenish the reserve fund if needed because of default by borrowers.

Example: The New Hampshire Municipal Bond Bank

The New Hampshire Bond Bank is a non-profit independent unit of state government administered by a board of directors. The bond bank, acting on behalf of local government units sells its own bonds, which are backed by a self-supporting reserve fund. The proceeds of the sale are used to make loans to participating governmental units.

Typically, the bond bank issues loans at least twice per year, with more frequent issuance if community demand exists. Each bond bank pool is backed by a self- supporting reserve fund set at a level equal to the maximum annual debt service. The reserve fund would be used for debt service in the event that any one of the participating governmental units defaults in its payments. The New Hampshire Bond Bank's bonds are not guaranteed by the State, but State law provides for the Bank to request an advance of State funds, at no interest cost, to maintain the legally required level of debt service reserve. The bond bank also has the ability to intercept a municipality's state payment should they default on their obligation to the Bond Bank.
The bond bank has made 884 loans to 230 local government units for a total of $1.2 billion since 1977. The largest individual loan was $32 million and the smallest was $19,000. The bond bank

issues both general obligation bonds, which are backed by the full credit of the underlying local government borrowers, and revenue bonds for public utilities and certain educational institutions. Bond bank staff review the annual budgets and audits of its borrowers to assure itself that its borrowers are continuing to maintain a fiscal balance.

Its most recent credit rating is Aa3 from Moody's and A+ from Standard and Poors. The majority of its local government borrowers do not have stand-alone credit ratings. In its 21 year history, no borrower has defaulted on its obligations to the bond bank.

The New Hampshire Municipal Bond Bank has a staff of three persons and an Executive Director. Its five-member Board includes the state treasurer, and municipal government and banking community representatives.

Example: The Puerto Rico Municipal Finance Agency

The Puerto Rico Municipal Finance Agency (MFA) was created as an affiliate of the Government Development Bank for Puerto Rico in 1972. Its stated purpose is to facilitate access to capital markets for the municipalities of Puerto Rico, so that they can bolster their economic self-sufficiency and reduce their dependence on central government funding. This strategy involves increasing the capacity of the municipalities to finance needed facilities through funds raised directly by bond issues.

The bonds of the MFA are rated by Moodies as "Baa1"and by S&P as "A-", similar to the rating of the Commonwealth of Puerto Rico itself. The MFA maintains a debt service reserve fund equal to 50 percent of maximum annual debt service. In addition, the MFA has received a "moral obligation" pledge of support from the Commonwealth in case of deficiency in the reserve fund. There is also a Commonwealth statute that requires each municipality to maintain a "redemption fund" in the Government Development Bank to cover its own debt service. This redemption fund is financed by a special surcharge on property taxes. Municipalities are restricted in borrowing to 10 percent of assessed property value. There have been no defaults nor calls on the reserve fund in the history of the MFA.

2. Water and Wastewater Revolving Funds

The US Federal Environmental Protection Agency has in recent years encouraged each state to set up "State Revolving Funds" for water and for wastewater. These revolving funds are a means of channeling federal and sometimes state subsidies to local governments for water and wastewater investments. Under these schemes, repayments of sub-loans made to local governments accrue to the state revolving fund and are available for re-lending, rather than returned to the US Treasury. Several states augment federal subsidies with their own state subsidies. A few water and wastewater revolving funds deposit the re-flows from earlier loans into a reserve fund to support bond flotations. In this way they leverage public finds in order to obtain additional private funding. A wide variety of institutions have been set up by individual states to manage the revolving fund. Sometimes the state bond bank also manages the water and wastewater revolving fund, and sometimes the revolving fund is managed independently.

Example: Pennsylvania Infrastructure Investment Authority (PENNVEST)

PENNVEST, a water and wastewater revolving fund is an independent agency of the Commonwealth of Pennsylvania. It was established in 1988 to provide loans and grants to owners and operators of sewer, water, and storm-water systems for infrastructure improvements. It has a thirteen-member Board of Directors, chaired by the Governor of the state. Members of the board include cabinet secretaries, legislators, local government officials, and representatives of the water industry. It has a staff of 21. Its capital comes from grants form the federal government ($700 million) and from the state of Pennsylvania ($1 billion). Loans and grants made by PENNVEST, when repaid by its sub-borrowers, remain in the revolving fund for further on-lending and are not repaid to the federal or state governments. PENNVEST also does limited borrowing from the capital markets.

In addition to loans, PENNVEST offers limited grants to communities that are extremely distressed financially. All aspects of a project are eligible for funding, including feasibility analysis, design and engineering, expansion, and new construction

A team of PENNVEST staff evaluates the credit worthiness of each loan and grant application. The state's Department of Environmental Protection also reviews the quality of the environmental design. In FY1999-2000, the PENNVEST board of directors met three times to approve 100 projects, for a total of $205.1 million in assistance. Of this $13.9 million was in the form of grants.

B. CANADIAN EXPERIENCE

The first municipal bond bank in North America was established in the Canadian province of Alberta in 1956, well before the first US bond bank was established in 1970 in Vermont. Currently, six of the ten provinces of Canada have a Municipal Financing Corporation (MFC). The MFCs operate in a manner similar to the US bond banks and have the responsibility for pooling the borrowing needs of local governments in the province and for borrowing on behalf of the local governments. The MFCs are established by Provincial legislation. In all Canadian provinces except British Columbia, the provincial government directly guarantees the bond issues of the MFCs. In the US, bond banks are generally not directly guaranteed.

Example: Municipal Finance Authority of British Columbia

The Municipal Finance Authority (MFA) of British Columbia is the central borrowing agency for municipalities and regional districts in the Province. The MFA was created by provincial legislation in 1970.

The stated reason for establishment of the MFA was "a recognition that it made economic sense for individual municipalities and regional districts to borrow together as a group and to guarantee each other's credit". The pooling of their borrowing would produce economies of scale by sharing the fixed costs of floating a bond. Officials also felt that the Province should function together as a unit, and that without the development of the smaller municipalities in the hinterland, the larger urban areas (such as Vancouver and Victoria) would not achieve the prosperity that they sought.

British Columbia is divided into 27 regional districts, each governed by a regional board consisting of representatives of its member municipalities and unincorporated areas. The regional boards appoint members to the Authority, based on the population of their regional districts. There are no provincial officials on the MFA Board of Directors and there is no guarantee from the Province.

The legislation that created the MFA was structured so that all municipalities contributed to a debt reserve fund whenever they borrowed. That contribution would not be returned to them until each loan was repaid 15, 20 or 25 years later. If the debt reserve fund were ever drawn down by a default of one or more municipalities, it could be replenished by a Province-wide tax levy. To date, this fund has never been drawn upon. Accordingly, there has never been a need for a debt-reserve-fund levy to be applied.

The MFA of British Columbia is presently rated Aaa by Moody's Investors Service and AAA by Standard & Poor's Rating Service.

By 1989, officials concluded that the structure and credit of the Authority could be used for purposes other than capital borrowing. As a result, the objectives of the MFA have been expanded to include a short-term investment fund (essentially a mutual fund which municipalities can invest in), interim financing, and pooled leasing for members. Municipalities use these financial products at their option, and they are contracted out for management by the private sector. The pooled interim financing program serves those communities that need funds in advance of tax receipts each year. The leasing pool provides leasing for any asset from photocopiers to tractors.

Example: The Alberta Municipal Financing Corporation

The Alberta Municipal Financing Corporation (AMFC) is a non-profit corporation established in 1956. Its stated aim is to assist municipal jurisdictions within the province to obtain capital funds at the lowest possible cost consistent with the financial viability of the corporation. It does this through providing municipalities with access to capital markets, which would not be available to municipalities on an independent basis. AMFC makes loans to municipalities, school boards and other local entities. Interest rates are based on its own cost of borrowing.

The obligations of the AMFC carry the unconditional guarantee of the Province of Alberta.

C. EUROPEAN EXPERIENCE

The evolution in Europe has been somewhat different than in North America. In Scandinavia, for example, several of the specialized municipal banks had their origin in initiatives by local government associations to pool their resources and lend to members, much as a credit union might operate. Many of the communal banks of Scandinavia are still partly owned by local governments. As these institutions evolved, national governments played more of a controlling role and in some cases have taken significant ownership shares.

1. The Scandinavian "Communal Banks"

Denmark, Norway, Finland and Sweden all have specialized institutions that lend to municipalities. They operate along principles similar to the bond pools of North America. A distinguishing characteristic is that for the most part, the financing institutions have a strong ownership link to the local governments that they support. KommuneKredit of Denmark was founded in 1899 as a cooperative owned by all Danish municipalities and Counties. Kommuninvest of Sweden was founded in 1986 and is owned by a cooperative society of 111 local authorities covering 32 percent of the Swedish population. Municipality Finance plc. of Finland was established in 1989 and is owned by the primary local government pensions institution. In Norway, Kommunal Bankan was established in 1999 (but is the successor to an institution founded in 1936) and is owned 80 percent by the Norway government and 20 percent by a municipal government pension fund.

Example: Kommuninvest of Sweden

Kommuninvest is a cooperative society of local and county councils. Membership in the cooperative is voluntary, but the applicant is subject to scrutiny. Members must buy capital stock to join. The cost is currently set at SEK 36 per inhabitant for municipalities and 18 SEK per inhabitant for county councils. The society's members sign unlimited joint and several guarantees to cover all credit liabilities of Kommuninvest. In case of a call on the guarantee, demands will be apportioned based on the individual municipality's liability to Kommuninvest.

Kommuninvest has adopted a strategy of frequent bond issues in order to ensure that its bonds and the Kommuninvest name appears frequently before market participants so that Kommuninvest is felt to be a known and trusted borrower. To reduce risks, the company lends exclusively to members of the cooperative society or to companies controlled by them. The terms for borrowing and lending are matched exactly. This matching helps the company to avoid interest rate and currency risks. When different currencies are borrowed, the policy is to cover the currency exchange risks through currency swaps. Interest swaps are also used to reduce interest risks.

Kommuninvest offers financial advisory services for a fee and also arranges training seminars in financial administration for civil servants at local government level.

Example: Kommunal Bankan of Norway

Kommunal Bankan of Norway is a limited company that lends to sub-national government units and local public service providers such as power plants, private health institutions, co-operative water works and other projects that perform local government services. When lending to publicly owned but independent public service providers, loans must carry a municipal guarantee and must be for primary municipal services.

The Bank was formed in November 1999 following a reorganization of its predecessor, a state agency called Norges Kommunal Bank, which was formed in 1926. The State has retained ownership of 80 percent of Kommunal Bankan, with 20 percent owned by KLP, the premier municipal government pension fund. The part ownership of Kommunal Banken by KLP was intended to give municipalities a voice in the corporate governance.

Kommunal Bankan is the largest lender to sub-national governments in Norway, with a total portfolio of just over US$ 4 billion in outstanding loans. Municipalities can also borrow from Norwegian commercial banks. Kommunal Bankan's very strong credit ratings allow it to access international capital at advantageous rates, and it is able to pass those savings onto its clients. Bond issues of Kommunal Bankan are not guaranteed by the state, but enjoy strong implicit support. Over the last 75 years, no sub-national government has defaulted on a loan to Kommunal Bankan or its predecessor. Standard and Poors gives it an AAA rating and Moodies gives it its highest Aaa rating.

Kommunal Bankan offers both fixed and floating rates of interest, and long maturities with fixed rates up to 10 years. Its short-term floating-rate loans are based on the funding costs for its shortest issues. It is not regulated by the Norwegian Commercial Bank Act and Savings Bank Act but supervised as a financial institution by the Banking, Insurance and Securities Commission.

Kommunal Bankan is interested in carving out a niche for itself in finance that involves public-private (as well as public-public) partnerships. Such partnerships are a growing trend in Norway as elsewhere

2. European Banks

In the last decade market liberalization has changed the character of municipal lending in Europe, opening it up to greater competition and increasing the number of institutions providing municipal credit, and bringing in mutual funds and insurance companies. In Germany, Spain, Italy and France lending has evolved from a situation where one specialized bank in each country provided most credit to its local clients, to one in which capital market access through bonds and project finance play an increasingly important role along with cross boarder banking entrants. Competition has lowered costs and fostered declining interest rates.

Example: Banco Credito Local (BCL)

In Spain, BCL was established in 1925 by a group of private bankers with a 40 percent ownership by Spanish Local Authorities. It was nationalized in 1962 and was re-privatized in a process that began in 1993 and ended in 1998. Following nationalization in 1962, BCL was funded directly by the Spanish Treasury. With deregulation, in 1991, it began issuing bonds. As a private institution, BCL has retained its specialized business of lending to local entities as part of the Argentaria group. It has begun to operate on a European-wide and even international level.

National regulations permit local borrowing. A local entity can borrow with city council approval if net savings are positive and if total debt is less than 110 percent of current revenues. Otherwise national and regional government approval is necessary and a three-year financial adjustment plan has to be approved by the city council.
Example: Dexia

In France, Credit Local de France (CDL), a publicly owned corporation, handled a large share of municipal lending prior to 1993 when it was privatized. CDL lent to municipalities for technical assistance as well as capital projects, and helped to arrange TA through its associated consulting companies. In 1995, Dexia, a private banking company, was formed to conduct municipal lending on an international level by a merger of Credit Local de France and Credit Communal de Belgique. France has removed most bottlenecks to competition among institutions that share municipal business. Dexia has about 40 percent market share in France.

Dexia operates through specialized subsidiaries, branches and agencies in a dozen countries. In Belgium, Dexia Bank has a market share of 79 percent of the local public sector business. It has acquired interests in local communal banks and other financial institutions in Germany, the United Kingdom, Italy, Spain, Slovakia, Sweden, and Austria. (It holds 47.6 percent interest in Kommunalkredit Austria). Dexia has emerged as a large, universal banking institution. In 1999 it provided its clients with almost 23 billion euros, bringing outstanding commitments to almost 110 billion euros. It's public sector operation has four main lines of business: making loans to local governments and public sector organizations; financing infrastructure projects through project finance or structured financing; enhancing the credit of municipal bonds through insurance and other products; and provision of a range of customized financial services, including account management, the optimization of financial flows, investment products, etc. It has over 2000 employees.

D. JAPANESE EXPERIENCE

The Japan Finance Corporation for Municipal Enterprises (JFM) provides long-term funds for public works projects. The JFM is fully owned by the Government of Japan (GOJ) and its debts are unconditionally guaranteed by GOJ. Its credit rating is therefore the credit rating of GOJ.

JFM raises funds principally through the issuance of publicly offered bonds, both domestic and foreign. JFM is exposed to interest risk, as the average maturity of its bonds is 10 years against loan terms that it provides of up to 28 years. Loans for sewage facilities and local roads account for the largest share of JFM's loan allocation. Virtually all villages, towns, and cities in Japan have borrowed from JFM.

The appropriate sector ministries approve all loans made by JFM. In turn, JFM's own borrowings to fund these loans require ministerial approval. JFM has never experienced loan loss.

The Japan Development Bank (JDB) also makes loans to regional and local government projects. JDB is fully government owned. It began lending for regional development in 1959 and for urban development in 1966. It usually lends 30 to 40 percent of project costs, with repayment negotiable up to 30 years. It has a special focus on large-scale public-private type projects. Its loans are designed to provide comfort to potential private sector investors and lenders and thereby to increase private participation. In FY 1997, JDB lent approximately 175 billion Yen for urban development and 182 billion Yen for regional development.

E. DEVELOPING WORLD EXPERIENCE

In the developing world, the origin of municipal lending institutions is quite different from that of North America, Europe, or even Japan. Developing countries often have underdeveloped financial systems with short tenors and high interest rates relative to the needs of the infrastructure projects that form the bulk of local government development needs. In a large number of cases, the specialized institutions that lend to local governments in developing countries were created with the support of multilateral development banks. Their purpose was often to channel ODA funding to local governments under the reasoning that the only way to channel ODA to the large number of local governments in need of assistance was to employ a local intermediary. Also the financial system of most developing countries was felt to be too weak to support market-based financial intermediaries.

Many of these institutions (e.g. PARANACIDADE in Brazil, FINDETER in Columbia, TNUDF in India, and MDFO in the Philippines) have done a very good job of initiating a credit culture among local governments, have strong repayment records, and have had a positive effect in improving the capacity of local governments to plan and implement projects. At the same time, some municipal finance institutions in developing countries have not been successful and have experienced high default rates and poor performance. Examples include the Kenya Local Government Loan Authority which had a non-performing rate of over 80 percent and is now essentially defunct, the Honduras fund which had more than 50 percent of its loans in non-performing status at one point, and the Indonesian Regional Development Authority (RDA) which has lent without requiring security from its local government borrowers.

Only a few institutions in the developing world have developed sustainable models for tapping private funds. INCA in South Africa, and the Tamil Nadu fund in India, are notable examples of institutions that have been successful in tapping private funding to support municipal lending. Both India and South Africa have fairly well developed domestic financial markets, which is an important factor in the success of these institutions.

Bonds have played a small role in financing local governments in the developing world, but domestic bond issues by local governments are gradually increasing in magnitude. It is unrealistic to expect more than a very small percentage of local governments of the developing world to issue international bonds (e.g. Buenos Aires, Rio de Janeiro). In some cases the prospect of a bond issue and the need for a bond rating can be a stimulus for broad management reforms. For example, the Ahmedabad Municipal Corporation recruited 40 MBA professionals to help improve the management of municipal systems including the city's information system, computerization of records, billing, collection, etc. as part of reforms needed to restore fiscal balance prior to obtaining a domestic credit rating.

1. Second Tier Institutions

While most institutions that have been created in the developing world lend directly to local government units, there are a few, such as Columbia's FINDETER and Czech Republic's Municipal Infrastructure Finance Company, that are second tier institutions which are designed to facilitate the transition from public sector borrowing by local governments to private sector borrowing. These institutions work by rediscounting loans made by private banks. While only a few countries have set up institutions to rediscount bank loans made to local governments, there are a number of rediscounting institutions that have been set up in the developing world to support private bank lending to housing.

Example: FINDETER, Colombia

FINDETER is an autonomous, quasi-public financial organization that operates as a second-tier bank by channeling its loans through approved primary lenders, mainly commercial banks. FINDETER does not lend directly to local governments. It is subject to the regulations of the Banking Superintendent. Its shares are held by the Ministry of Finance (86 percent) and by regional governments (14 percent). FINDETER is intended to be an institution that encourages policy reforms in municipalities. Loans therefore require a double approval: first by FINDETER, which does a "rapid appraisal" of technical, economic and development issues based on checklists and cost comparators, and second by the commercial bank that takes the credit risk, which does a financial analysis. FINDETER's loan approval is often conditional on the municipality undertaking policy reforms such as tariff increases.

FINDETER rediscounts up to 85 percent of the total loan amount from the primary lender, requiring the primary lender to provide 15 percent of the loan amount from its own resources. The main benefit, which FINDETER provides to participating banks, is one of term transfer. It allows banks to lengthen the term of its loans without incurring a maturity mismatch. FINDETER lends to primary institutions at 2.5 percent over an index of bank deposit rates. It has recently eliminated the ceiling on the rate at which primary lenders can on-lend to local governments. Lenders are now free to negotiate with individual sub-borrowers, thus pricing their loans in accordance with specific market conditions. Tenors of FINDETER loans to banks are 8 to 12 years, which is much longer than the tenor available through normal commercial loans of 3 to 5 years. The primary lenders keep 100 percent of the credit risk on the entire loan. The main collateral for local government loans made by the private lenders is the pledge of revenue transfers (a voluntary intercept) due from central government to local governments, and in the case of revenue generating projects, revenue from tariffs or fees.

Since its creation in 1989, FINDETER has financed roughly US$1 billion in loans to over 700 municipalities, about 60 percent of Colombia's municipalities. Its loans have financed water and sewerage systems (35 percent of loans in 1995), urban roads (29 percent), schools (17 percent), and parks and markets. It can support not only local governments, but also their agencies or enterprises, including private or mixed capital companies operating on behalf of local governments. Maturity and grace periods for sub-loan amortization are established for each sector of investment, with maximums of 12 and 3 years, respectively. There have been virtually no late payments and no defaults from primary lenders to FINDETER. Commercial banks that lend to municipalities are often depository banks for the municipality, which improves loan security. Municipalities are required to provide counterpart funds of at least 30 percent of project cost.

In addition to provision of a rediscount facility to banks, FINDETER in the past was contracted by the government to administer grant programs. This was handled under separate accounts and costs of grant administration were recovered from fees. Over time, there was some politicization of the grant making facility and a decision was taken to separate grant making from the credit function.

Technical Assistance to municipalities for capacity building is the responsibility of the Ministry of Planning. Consultant firms have been hired by the Ministry to provide outreach to smaller towns in a given region to help in planning, project development, and project implementation. Larger towns are expected to prepare projects with less Government support. However FINDETER itself does provide technical assistance in sub-project analysis, contracting, project supervision, etc. The government has given FINDETER a prominent role in its social sector strategy, and is counting on FINDETER to help galvanize private sector participation in urban services.

The Government of Colombia has repaid the debt service on loans made to FINDETER by multilateral development banks, in order to contribute to its capitalization. Equity now accounts for 48 percent of its funding, compared with banking norms that require a minimum of 9 percent for financial institutions. This gives FINDETER considerable room to leverage its equity with more loans.

FINDETER has about 180 staff. Its employees have salary and benefits that are in line with banking sector comparators, enabling FINDETER to engage first rate professionals.

FINDETER has been successful in introducing private banks to the local government market. With the good performance of their local government portfolio, private banks have increased local government lending using their own capital without FINDETER support. The subsequent competition among private banks has led to a lengthening of tenors available to local governments. The larger municipalities often utilize the private banking system, which is faster and less bureaucratic, while smaller municipalities use bank loans supported by FINDETER, which still have longer maturities than unsupported private loans.

2. Municipal Development Funds

Among the institutions that lend directly to LGUs are the municipal development funds of Brazil, India and South Africa.

Example: PARANACIDADE in Parana State, Brazil

The Municipal Development Fund of Parana State in Brazil was set up in 1981. Until 1996, it was managed by a state agency within the Secretariat of Urban Development. In 1996, in order to improve management of the fund, management was contracted out to a non-profit independent institution called PARANACIDADE that operates under private sector rules. PARANACIDADE's private sector legal status allows it to operate flexibly and efficiently. PARANACIDADE has the responsibility for managing the "Urban Development Fund" (FDU). The resources of the fund are owned by the State and derive mostly from re-flows from earlier World Bank and InterAmerican Development Bank (IDB) loans. The State assumed the repayment obligation of these loans while allowing the re-flows from loans to municipalities to remain with the fund. This provided funds for the capitalization of the FDU, which now operates as a revolving fund. Any new loans made by multi-laterals or other sources to the FDU, since the contracting out of its management, (including new loans from the multilateral development banks) must be repaid by PARANACIDADE. This exposes it to interest rate exposure. In 1999, a devaluation of 48 percent led to a loss in capitalization of R 88 million.

The fund can lend to municipalities, associations of municipalities, and utilities owned by municipalities. It cannot lend to private utilities or private infrastructure service companies, although there are proposals to change regulations to permit this. PARANACIDADE requires municipalities to pledge the transfers from state government due to the municipality as security for any loan.

PARANACIDADE does not do extensive, independent assessments of the development impact of a particular project relative to other projects, but rather relies on the judgment of local officials. It does make its own projections of local ability to repay. An interesting feature of its lending is the use of local associations which are themselves authorized by PARANACIDADE to screen projects from individual members of their region of the state. This has proven to be a successful method to promote local responsibility.

PARANACIDADE provides technical assistance to municipalities for capacity building. Subjects that are covered include administrative management, urban planning, tax and financial management, and information systems. Technical assistance is currently provided to municipalities on the basis of 40 percent loan and 60 percent grant.

Example: Tamil Nadu, India

In 1988 the Government of Tamil Nadu (GOTN) State in India established a Municipal Development Fund (MUDF). By October 1996, the MUDF had financed over 500 sub-projects including roads, bridges, street lights, solid waste plants, storm water drains, bus stations, and markets in 90 out of 110 municipalities in Tamil Nadu. It disbursed about Rs.1, 650 million

(US$ 63 million at average exchange rate). The MUDF had been generating adequate profits from the satisfactory spread and high rate of loan repayments, which were a result of adherence to well-defined lending rules and procedures.

Although the MUDF had proven itself as a relatively successful municipal credit scheme, it had a number of shortcomings: (i) its lending capacity was far too small compared to the potential demand for urban infrastructure investment; (ii) it depended entirely on public financing (iii) it was located within the administrative machinery of the Government, and faced potential risks of political influence; and (iv) its staff was not free from the general constraints of the civil service system, such as salary and hiring regulations.

In order to overcome these shortcomings, the GOTN decided to restructure the fund. The major objective of the restructuring was to convert the Municipal Urban Development Fund into an autonomous financial intermediary (called the Tamil Nadu Urban Development Fund (TNUDF)) with the participation of private sector capital and private sector management. The new fund, which is government, owned, is managed outside government by a private fund management company called the TNUIFS. Additionally, a new Grant Fund (GF) was set up to encourage urban infrastructure investments targeted to the urban poor, and to finance technical assistance, resettlement and rehabilitation costs. The grant fund is also managed by the TNUDF.

At the reorganization, the scope of operations was widened to include urban infrastructure projects sponsored by private investors. The grant fund also finances technical assistance costs for local governments.

The main purpose of the TNUDF is to channel increased financial resources, including private financing, into high priority infrastructure investments, mobilize resources from the capital markets; facilitate the participation of private sector in infrastructure development through direct investment; and improve the financial management of urban local bodies, enabling them to access debt finance from markets. The Government of Tamil Nadu’s equity is restricted to 49 percent in order to facilitate private sector management in investment decisions.

The participating private institutions have committed US$12 million as their share contribution to the TNUDF. In addition, they have agreed to mobilize US$25 million in the form of co-financing of sub-projects of the TNUDF. They have also agreed that they would assist the TNUDF in raising an additional US$25 million from the capital market by underwriting or guaranteeing the TNUDF debt or by providing other credit enhancement/risk participation mechanisms. The ICICI, a major domestic financial institution, is supporting the TNUDF by seconding key management staff. Others are extending technical support to the TNUDF on a project-by-project basis.

Bonds issued by TNUDF are not guaranteed by either the state or the national government. Based on its initial three-year track record, the TNUDF recently was successful in mobilizing Rs 1billion through a domestic capital market issue.

Some of the institutional development and capacity building functions of the former MUDF are being implemented by the Tamil Nadu Institute of Urban Studies (TNIUS) under the supervision of the Department of Municipal Administration and Water Supply (DMAWS). These institutions will strengthen the managerial, financial, technical and procurement capacity of local government units through training and technical assistance. An important element of the institutional development program of the government is to assist local governments in the preparation and implementation of their City Corporate Plan (CCP).

Example: The Infrastructure Finance Corporation Limited (INCA) of South Africa

INCA is an infrastructure debt fund in South Africa that is 100 per cent privately owned and operated. It was established following a call by the South African government for increased private sector involvement in infrastructure funding. The main funding sources it draws on are local and international market funds, raised through a series of INCA bond issues and long-term loans. Another source of funding available to INCA is shareholders' capital. In the future it will also have funding available from the issue of Junior Bonds. Commitment to these has already been obtained. INCA's borrowers include municipalities, water boards and other statutory institutions in South Africa whose main business is the establishment of social and economic infrastructure in South Africa. This funding has mainly been in the form of long-term fixed interest rate loans.

INCA's loans vary between five to thirteen years, depending on the repayment profile of funds raised by INCA itself on the local and international capital markets. Normally, INCA would have a number of different sources of funding available, and the most suitable option would be offered to the borrower. Typical long-term funds available on the capital markets require six-monthly interest payment with a bullet capital repayment. INCA loans can also be amortized.

INCA is actively involved in efforts to build capacity at local government level. With assistance from the French Government, INCA established the "French Fund" to finance capacity building efforts on a grant basis. INCA also assists local authorities with long-term financial planning, and has a forecasting model to assist municipalities to calculate maximum levels of affordable borrowing.

F. LESSONS FROM INTERNATIONAL EXPERIENCE AND APPLICABILITY TO THE PHILIPPINES

The key ingredients of a well functioning local government credit system are:

- A decentralization process that gives autonomy to local governments and that balances the service delivery responsibilities of local governments with the sources of revenue available to them;
- Revenue flows to local governments that are predictable over time, which involve significant local control, and which allow long term budget forecasts and loan repayment forecasts to be made;
- Good management systems including well designed, transparent procedures for investment planning, procurement, operations, maintenance, budgeting and financing, and trained professional staff to implement the management systems;

- Modern accounting, auditing and disclosure standards for local governments;
- The timely provision of comprehensive public information about budgets, finances, and debt in a format that is uniform across local governments;
- Policies that promote private, corporate style operation of public services and which carefully manage the contingent liabilities assumed by local governments; and
- Policies, and a legal, regulatory and tax system that promote a competitive, level playing field among private and public financial institutions, that promote competition between bonds and bank loans, and that are flexible in accommodating the needs of new financial products.

With these basic ingredients in place, supporting institutions will emerge over time including private credit rating agencies; bond insurance companies, secondary trading institutions, etc.

The Philippines has some of the above ingredients in place, but not all. The 1991 Local Government Code (LGC) has been an excellent blueprint for decentralization of responsibility to local governments. The internal revenue allotment (IRA), which was implemented under the code, has given local governments a stable, predictable flow of revenues which in the past ten years have led to a high quality portfolio for the GFIs that have made loans to local governments. A revenue equalization formula such as the IRA has been an essential first building block for local finance in many countries, and enables a local government to provide security to its loans by a pledge of these receipts. Future changes in the IRA formula might be in the direction of providing enhanced incentives for local governments to increase own revenues as a percentage of total revenues. The 1991 LGC gives significant opportunity to local governments to raise their own revenues, but incentives to use this opportunity have not been strong. Most local chief executives rely heavily on the IRA, neglecting the opportunities that exist to increase revenues through local taxes and user charges. Improving their ability to raise their own revenues will lead banks and financial markets over time to rely less and less on the IRA, which is a national income source, as security for loans and more and more on the inherent fiscal management performance of individual local governments. This would be a positive sign of true decentralization. A modern accounting system is being put in place in the Philippines. The government has also started programs that promote private sector management and operations of public services at the local government level. While this is slow to take off, there is some initial progress in the water sector. More can be done to promote the use of private concessions in other types of revenue generating enterprises sponsored by LGUs.

The areas that deserve the most attention from the government are:

- The development of a comprehensive public information system on local government finances and local government debt;
- Removal of the bottlenecks to private bank lending to LGUs and leveling the playing field with the GFIs; and
- Systems that promote good management and planning.

In modern local government finance systems, bank loans to local governments coexist with a municipal bond market. While a country's macroeconomic circumstances determine its interest rate structure, evidence from Colombia has demonstrated that even in less advanced economies, competitive systems with multiple sources of finance for local governments will promote longer tenors and lower margins and therefore lower interest rates, other things being equal.

The Philippines is also fortunate to have a private local government bond insurance agency, the LGUGC. To date, the existing volume of business has not warranted the establishment of a private credit rating agency, but this could change if volume increases and costs are reduced through better LGU information reporting systems. The GFIs and LGUGC have developed their own credit scoring systems that are used in making their own credit decisions, but independent, private ratings would increase investor confidence in the risk analysis of individual local government securities.

1. Role of Specialized Lending Institutions

Institutions that specialize in lending to local governments are common in market economies with advanced financial systems as well as in developing economies with less advanced systems. In developed countries, they compete with other financial institutions and typically raise private money on the financial markets for re-lending to municipalities at market rates rather than directly lend public money. Many are bond-pooling institutions that borrow on behalf of weaker or smaller local governments. The security of the credits of these institutions is enhanced by the use of voluntary intercepts and by the use of reserve funds that typically cover at least one year's debt service. Some institutions also benefit from guarantees or implicit support from state level or national governments.

Specialized municipal financial institutions in developing countries that lend to Local governments, such as the MDFO, generally obtain their funds form ODA sources, and few have managed to change into institutions that utilize domestic markets to mobilize private funds. The Tamil Nadu fund of India is an exception. Other funds in the developing world clearly need to adopt a plan for moving in this direction if their activities are to be sustainable. The investment needs of local governments are far too great to be supported by ODA or other public funds over a long period. Long-term sustainability suggests shifting to using the domestic capital markets as sources of funds for domestic borrowing. ODA funds could facilitate this by helping to support domestic institutions that tap domestic markets. There are many ways to achieve this. Examples are providing increased security to domestic institutional borrowings through backup guarantees or providing facilities to lengthen tenors.

2. Management Structure

While many specialized intermediaries even in developed countries are publicly owned, most successful institutions in the developed and in the developing world have independent boards of directors, a corporate structure, and offer competitive salaries to attract professional staff. There are many variations, including a non-profit, corporate entity such as PARANACIDE in Brazil, or private management under a mixed board of directors as is common in Europe, and as exists in Tamil Nadu Fund in India.

The GFIs in the Philippines, though not dedicated to local government lending, are expanding their LGU portfolio and are developing specialized knowledge of local budgeting which is necessary to perform credit analysis of loans for LGUs. The MDFO, which is dedicated to LGU lending, is still building up its capacity, following the first phase of its reorganization. The present management of the MDFO is not corporate, which experience elsewhere indicates is essential. The shift to corporate management for the MDFO either directly through a management contract or indirectly through utilization of the GFIs is a possible outcome of the second phase of the MDFO reorganization.

3. Technical Assistance

Technical assistance provided to local governments by the specialized lending institutions in advanced economies is limited and usually covers only assistance in understanding how to use the facilities provided by the financing institution. There is little economic or social evaluation of projects, and the assumption is that there is no need to second-guess local priorities.

4. Grants

Municipalities in developing countries require more extensive technical assistance for capacity building, feasibility studies, procurement, environmental and social analyses and monitoring than is true in the more advanced economies. Line agencies typically have responsibility for general capacity building and training, with municipal lending institutions offering limited technical assistance. Many local governments are not willing to borrow for general capacity building and seek grants from higher levels of government. The municipal lending institutions typically offer technical assistance for project feasibility studies, procurement and matters related to the success of projects being financed. Often, local governments borrow for this technical assistance, but sometimes there is partial grant support from national government. Generally, it is desirable for local governments to have equal access to needed technical assistance no matter what source of financing they decide to pursue. National governments also often finance grants to certain categories of projects justified by the positive externalities where there are social and environmental benefits. In developed countries, the affordability and financial sustainability of large-scale grant programs needs to be considered, but unfortunately, financial sustainability rarely receives the attention it deserves in the design of subsidy schemes. Several countries (Colombia, Poland, Tamil Nadu) have changed their institutional approach to grant making and are unbundling grant making authority from credit making authority. This is to avoid delaying the entry of private lending by offering inducements only available through a public sector lending institution. There may also be possible moral hazard in giving grants along with loans where the lending institution might be tempted to bend the criteria under which it makes a grant in order to make a loan.

The applicability of some of the above lessons for the MDFO are considered further in the following section.

IV. STRATEGIC ROLES AND DEVELOPMENT OF THE MDFO

The TOR asked the consultants to "…define the role of MDFO in fulfilling local government financing needs vis-à-vis other financial institutions. From this evaluation, strategic options for the role and development of the MDFO in the medium – term will be recommended."

A. COMPLETING THE PHASE ONE` RESTRUCTURING OF THE MDFO

Background

The Municipal Development Fund (MDF) was established in 1984 by Presidential Decree No. 1914 as a revolving fund for ODA-supported projects intended to help promote self-reliance of local governments in undertaking socio-economic development. Its major objective was to establish an effective system to make international assistance available to local governments through the national government.

Through the years, the MDF became a very important channel of ODA funds intended for local governments. Foreign-assisted projects with a total value of over US $1.7 billion have been implemented through the MDF during the past ten years, and are at various stages of implementation. The value of MDF's portfolio of existing sub-loans to LGUs amounts to about 3.5 billion pesos from some 189 active loans as of 2001. Of these, 69 LGUs are classified as 3rd to 6th class LGUs.

The MDF was originally located within the Bureau of Local Government Finance (BLGF) of the DOF. BLGF staff handled coordination and administered loan disbursement for the MDF, but not technical analysis of projects, over and above their other duties. Technical analysis, including project identification, supervision of feasibility studies and appraisal was handled by staff located in Central Project Offices (CPOs) which were established for each donor funded project and were located in the lead line agency concerned. For example, the municipal development projects supported by the World Bank had the CPO located in the Department of Public Works and Highways (DPWH).

The MDF performed well in achieving its objectives according to a report of the Operations Evaluation Department of the World Bank (*Developing Towns and Cities: Lessons from Brazil and the Philippines*, OED, 1999). This evaluation found that participating municipalities improved their fiscal and financial performance significantly in comparison with similar but non-participating municipalities.

However, with the growing number of foreign-assisted projects being designed to involve LGUs, not just in project implementation but also in co-financing sub-projects, there was a felt need to have full-time staff who would be able to do both technical and financial appraisal within the same office. In 1998, a decision was taken to launch a two-phased restructuring of the MDF. The first phase was launched on November 20, 1998 when the President of the Philippines signed Executive Order No. 41, which reorganized the administrative structure of the MDF and created the Municipal Development Fund Office (MDFO) as a separate office of DOF. After the reorganization, the MDFO was to have its own full-time staff (relying on former staff of the participating line agencies who had worked on MDF projects to allow for continuity of expertise) and have the CPOs housed within the MDFO itself.

The second phase of the MDF restructuring was to involve the spin off or transfer of the MDFO out of the DOF to an existing or a new financial institution. It was agreed in the LOGOFIND project agreement with the World Bank that a decision on the various options for "spinning off or transfer" would be made by December 2000 and actual spin-off or transfer was expected to be completed by March 2003.

The rationale for the second phase is that, as a lender, the MDFO needs to be able to make judgments about the creditworthiness of a project based on the merits of the proposal and the creditworthiness of the concerned LGU. It should act quickly and bear the consequences of its credit decisions. Exercising a credit making function would be better undertaken in a corporate style, banking environment rather than in a unit of a government department. It is also the Government's policy that credit functions should be transferred from government departments to GFIs to improve the commercial basis of these loans.

Issues and Concerns

1) Strengthening MDFO Capacity

Under the first phase reorganization that created the MDFO as a separate unit of DOF, MDFO's capacity was to be strengthened by hiring its own professional staff so that it would not be entirely dependent on the national line agencies for project analysis and appraisal, and so that it could develop its own specialized expertise. This did not happen as planned. MDFO was not given authority to hire the staff it needed to carry out its mandated functions. This was in part because of a hiring freeze imposed by the Office of the President. The staffing structure that was proposed by DOF contains 79 regular positions. To date, MDFO has been given only 39 contractual positions. Thus, MDFO has not been fully equipped to perform its mandated functions and delays in ODA projects have been experienced.

The MDFO has also been affected by competition from the GFIs. In the years since the LGU Financing Framework was put in place, lending to LGUs by the Land Bank and Development Bank of the Philippines had increased dramatically. This has created some overlap in areas of lending. Also, the GFIs have become important channels in their own right for ODA funds to local governments. MDFO, however, is the only institution that channels both grants and loans to LGUs.

Recommendation:

In order to fully realize the benefits envisioned from the foreign-assisted projects that are being channeled through the MDFO, it is of utmost importance that the manpower requirements of the MDFO be met as soon as possible through the provision and filling up of regular plantilla positions. Recourse to the hiring of consultants may be eventually more expensive for the government and does not allow the building up of internal capacity or institutions. It also runs counter to one of the objectives of the MDFO reorganization which is to safeguard the fiscal health of the national government which will have to repay all the loans coursed through the MDFO. Present use of contractual employees for accounting responsibilities within the different projects is undesirable. It is therefore urgently recommended that plantilla positions be approved for all budgeting, accounting and internal auditing functions. The same would hold true for project appraisal teams since the non viability of approved projects would make it difficult for the concerned LGUs to repay back their loans to the MDFO and the national government will have to pay for the foreign loan with its very limited resources, upon which there are many competing demands.

To make the operations of the MDFO as efficient and effective as possible, a needs assessment and intensive training of all personnel in LGU finances, credit processes, project preparation and appraisal, and marketing and communication skills should also be undertaken. No effort should be spared in speeding up the computerization of existing loan and grant records, from the beginning of the MDF in 1984, and setting up of a management information system for new projects and programs. Loan and grant disbursement procedures would also need to be streamlined and formal performance and financial auditing procedures instituted. These are necessary to speed up the implementation of projects while at the same time ensuring that transparency and accountability are safeguarded.

2) Sharing Responsibility for Capacity Building in LGUs

Critical to the success of any project involving LGUs is the capacity of the LGU to properly prepare for, implement and sustain the gains of a project. In addition to financing resources for capital projects, the MDFO currently manages considerable funds for technical assistance to LGUs. There are other government agencies that also have responsibility for providing technical assistance and capacity building activities for LGUs.

Recommendation:

The sharing of responsibilities should be worked out with the Department of Interior and Local Governments and its Local Government Academy and the NEDA for general capacity building and local development planning, respectively, and concerned national government agencies such as the Department of Environment and Natural Resources, Department of Agriculture and Department of Public Works and Highways for sector-specific technical assistance. The MDFO can play a coordinating role so that LGUs are able to secure all the technical assistance that they need to identify, prepare and implement their priority projects.

3) Enhancing MDFO's Role in Promoting Private Sector Financing for LGUs

MDFO was to play a key role in promoting private sector financing for LGUs and facilitating the graduation of LGUs up the scale from GFIs to private lending. Since launching the framework, MDFO has not managed to undertake any specific action to promote private lending. It has tried to avoid competition with private lending by limiting its lending primarily to lower tier LGUs. As noted earlier, however, the GFIs, which hold advantages over private banks in that they are allowed to be depository institutions of LGUs have increased their lending to LGUs. Graduation to private financing has not occurred, apart from a few bonds floated by the LGUs and guaranteed by the LGUGC. It is clear that additional measures will be required for MDFO to play a key role in promoting private lending.

Recommendation:

Since much of the funding for LGU lending by MDFO and even the GFIs originates with multilateral and bilateral donors, there may be the possibility of MDFO to work with the providers of ODA funds to more actively promote private domestic lending to LGUs through innovative project design. Two models should be considered: one a model under which MDFO acts as a re-discounter of commercial bank loans, the other in which MDFO acts as a bond bank. International experience with these models was discussed earlier. The possible application of these models in the Philippines is discussed below.

MDFO could also play a more proactive role in monitoring the implementation of the LGU Financing Framework. It would be ideal to–have specific MDFO personnel assigned to make sure that the various measures identified in this report to remove the bottlenecks to private bank lending to LGUs, bond flotation or BOT arrangements with LGUs are implemented in a timely manner so that the ultimate objective of the Framework to graduate LGUs to the private capital markets will be realized as soon as possible.

B. OPTIONS FOR THE PHASE TWO REORGANIZATION OF MDFO

As mentioned earlier, the second phase of the MDFO reorganization is intended to spin off or transfer the MDFO out of the DOF into an existing or new financial institution in order to reduce the bureaucratic constraints on MDFO and to increase accountability of management for lending decisions.

1. Three Early Options for a Municipal Development Fund Corporation

In 1998, as consultants of the DOF, C. Virata &Associates, Inc. proposed that in the second phase of the MDFO reorganization, the MDFO would evolve into an LGU financing institution with its own corporate personality. Thus, the MDFO would become the Municipal Development Fund Corporation. Three options for corporatizing the MDFO were presented and analyzed. They were the following:

a) Transferring the management of the Municipal Development Fund (MDF) to a subsidiary of an existing GFI;
b) Transferring the assets and liabilities (and the risks) of the MDF to a subsidiary of an existing GFI; or
c) Creating a new GFI or municipal development bank to own and operate the MDF.

Option (a):

The first option refers to the transfer of the management of the MDF or Fund from the MDFO to a GFI subsidiary. A fiduciary relationship would be formed between the Department of Finance and the mother GFI where the mother GFI becomes the trustee of the Fund and a subsidiary is created to manage the Fund in order to fulfill the conditions of the agreement/contract. Under this arrangement, the DOF would still maintain ultimate control of the Fund since it would still legally belong to the DOF. Furthermore, oversight over the subsidiary's policies and procedures could be maintained by requiring that a Board of Directors be set up for the subsidiary with composition specified by DOF. One possibility would be for the Board's composition to be similar to the MDFO's current Policy Governing Board. As the owner of the Fund, the DOF could insist on this arrangement as part of the trustee agreement. Under this option, the credit risk remains with the Department of Finance, which would mean that the National Government would still be responsible for servicing the debts of the Fund. Two Manila-based World Bank officials, T. Hashimoto and L. League, and their consultant, G. Llanto, proposed a variant of this arrangement, under which the GFI would have a management contract to administer the Fund. While essentially similar in its substantive effects, a management contract has the further advantage in that changes can be easily made at the end of the contractual period if difficulties arise.

Given the fact that the GFIs have their own profitable lending operations, there could be a conflict of interest (or the perception of conflict of interest) between the GFI's mainline LGU lending and the lending of the new subsidiary. There is a danger that the GFI would not have an incentive to manage the Fund in a way that would allow it to prosper-- since LGU lending by the subsidiary could be seen by GFI management as coming at the expense of lending by the GFI itself. It would therefore be important to isolate the management of the Fund from the management of the mainline GFI operations. Only if the management of the subsidiary were fully independent from the management of the GFI would this option be viable. Having the trustee GFI establish an independent Board Directors of the Fund may accomplish this.

Option (b):

The second option can be considered if the DOF finds the trade-off between retaining control of the Fund and continuing to assume the credit risk unattractive. In this case, both the management of the Fund and the Fund itself will be transferred to the GFI subsidiary. Under this option, the DOF would relinquish control of the Fund along with the credit risk to the subsidiary corporation. Because of the conflict of interest issue mentioned above between the GFI's mainline LGU lending operations and the LGU lending by its subsidiary, it is equally important that the Fund, after transfer to the new subsidiary, be managed independently of the GFI's mainline LGU lending operations. The terms of transfer are therefore quite important. It would be necessary that the charter of the new subsidiary ensure independent management and an independent Board. Once the Board is established, the DOF would have no say in the policies and procedures of the subsidiary corporation, unless it were itself a member of the Board.

Some support activities to LGUs may be affected under this option. These include training programs and other LGU capacity building activities. Since the new subsidiary corporation will have to assume the credit risk, it will have to balance the cost and management burden of provision of LGU support activities against other banking activities that more directly contribute to the achievement of its corporate viability and profitability targets. On the other hand, the financial burden to the National Government is reduced.

Option (c):

The third option of creating a new GFI or municipal development bank is permitted under Philippine law since "government-owned or controlled corporations may be created or established by special charters in the interest of the common good and subject to the test of economic viability." (Article XII, Sec. 6, Philippine Constitution.) Creation of a new GFI must be accomplished by legislation. New legislation of this type is likely to require a very long time and would have uncertain results. In addition, this option faces the hurdle of overcoming government policy aimed at limiting the number of government-owned or controlled corporations. However, this option eliminates many of the problematic incentive issues of the first two options. It should be noted that in market economies, GFIs that specialize in market based lending to local governments, and which compete for funds on the market, are the norm. Given the importance of a properly functioning municipal finance system, and the need to adopt an approach that will facilitate the step by step introduction of a market oriented system based on international experience, this option could be considered for the longer term.

General considerations:

Another factor to be considered under the three options above is that the MDFO administers grants in addition to loans. GFIs are presently not permitted to channel national government grants to LGUs. Under the first option, since the Fund would continue to be owned by the DOF and would have a separate legal personality from the managing GFI, the GFI could be allowed to release grants on behalf of the Fund. The legal and policy framework for this option would need to be studied more carefully. If, however, it were deemed feasible, one could still have the situation that exists at present where a loan for a school made by the GFI under its mainline operations would not qualify for a grant, while the same loan made from and on behalf of the MDF would qualify. The recommendation that the administration of the Loan-Grant–Equity scheme be changed so that eligible projects can benefit without prejudice to the source of lending applies to this case.

Another matter requiring further study is the development of lending guidelines for the mainline GFI and its subsidiary to segment the market in a way that would eliminate the conflicts of interest cited under options (a) and (b) above but not bring about other issues such as concentration of credit risk in one lender. For example, it would be possible to develop lending guidelines to clarify the conditions under which a loan to an LGU would be made by the GFI itself and when the loan would be made by the subsidiary. Segmented lending guidelines could even be seen to support the graduation policy of the LGU Financing Framework, which defines different roles for the MDFO and the GFIs. While the MDFO and GFIs should have different roles, differentiation based on lending guidelines has some pitfalls. For example, lending guidelines could be based on the credit quality of individual LGUs; e.g. the GFI mainline operations could be given responsibility for better quality risks, and the MDFO responsibility for poor risks. However, this is not recommended. Both the GFI and the MDFO need to make credit decisions based on ability to repay. In the absence of an independent credit rating agency, it would be difficult to develop clear rules that differentiate the credit risk profiles that the two institutions would serve in a way that did not pose serious credit issues. If MDFO lent only to LGUs that were truly high risks, the danger is that the MDFO could be saddled with non-performing loans. This would set a very bad precedent. Currently, the MDFO has close to zero non-performing loans. Maintaining a prudent lending policy by the MDFO is critical to long-term success. The existence of defaults on LGU loans would be observed by the private sector and could set back the introduction of private lending to LGUs. If an LGU is in such bad financial condition that there is a significant risk of default, and yet is deserving of capital, then it may be better that funds be provided under a grant program of the government rather than as a loan.

Another way to develop credit guidelines could be to differentiate lending responsibilities between the Fund and its parent GFI on the basis of the income class of the LGU. This approach could be workable, even though today the GFIs are already lending to lower tier LGUs on the strength of the IRA pledge. The difficulty is that it would arbitrarily restrict the choice of lender by LGUs.

2. Management Contract with a Private Non-Profit Institution

The variant of option (a) above of a management contract with a GFI has already been mentioned. The conflict of interest issues that were discussed would be avoided entirely if the contract were made with an institution that is not itself already making loans to LGUs. A management contract could be put out for bidding among private groups or specially created corporations. If legislation or government regulations do not allow profit making entities to administer government grant programs, then the bidding for the MDFO management contract could be restricted to private non-profit institutions.

Alternately, the corporatized management of MDFO could administer loans only and grant programs could be left to DOF itself. What is most important is that seasoned managers with the appropriate expertise be allowed to manage the MDFO in a corporate style environment, unburdened by government rules and procedures. The management contract could specify the targets and outputs that need to be delivered and provide for quick means of changing the managers should they fail to do what is expected of them. As in option (a) above, the ownership of the MDFO and the Funds would remain with the national government. Only its management and operations would be contracted out, in this case to the private or non-profit sector. As mentioned earlier, this type of arrangement has been working out well in Brazil (PARANACIDE) and India (Tamil Nadu Fund). Lessons from these experiences can be more fully studied to see how they might be applied to the Philippines.

If establishing a management contract for the MDFO with the private sector were interpreted as establishing a new GFI, it would require new legislation and could be seen as having the same pragmatic difficulties in the short term, as option (c) above.

3. Transfer Retail Credit Functions to GFIs and PFIs

Corporatization of the retail lending function of MDFO can also be accomplished by simply transferring the retail lending function to one or both of the GFIs and eventually the PFIs and having the MDFO concentrate on other functions. The GFIs are government owned corporatized institutions that already lend to local governments. Giving them increased responsibility for being a channel for ODA lending to LGUs would be a relatively minor change. In this case, the GFIs would handle new lending that is now the responsibility of the MDFO as part of the GFIs' mainline lending operations, and not through a subsidiary. The GFIs would be fully responsible for their own credit analysis and for bearing credit risk. The MDFO should continue to service and be responsible for past credits and could retain its other current functions such as grant making, plus other new functions to be discussed below.

The GFI or PFI would appraise projects and decide whether to make a loan or not based on its existing credit criteria. Since many current ODA supported projects handled by MDFO are programs supported by national line agencies, the GFI or PFI would also have to agree to follow the policy guidelines of the national line agency as a supplemental guideline used in making loans. For example, in the case of LOGOFIND, funds would be limited to 3rd to 6th tier LGUs except for social and environmental projects, etc. Given the rapid increase in lending to LGUs by GFIs that has taken place, and given that GFIs are already lending to a wide variety of projects in lower tier LGUs using ODA funds, it would seem that the GFIs could manage MDFO funds as part of their mainline operations in a manner consistent with the MDFO's current lending policy.

There is some concern that the GFIs may not have the capacity to manage the additional workload. However, as noted above, the MDFO itself does not presently have sufficient capacity. It may be easier for a GFI to add capacity than MDFO. In any case, the GFIs should be asked to compete for the current ODA programs of MDFO and should detail in their proposals how they would handle capacity issues. Another concern is whether the GFIs would be able to handle development issues, and whether they would be able to handle environmental and procurement requirements of the multilateral development banks, which are the source of most ODA for LGUs. In recent years, the GFIs have been given significant responsibility by the multilaterals. Through projects such as the *LGU Urban Water and Sanitation Project* of the DBP and the *Water Districts Development Project* of the LBP, the GFIs have begun to learn how to handle the environmental and procurement rules of the multilateral development banks. It is clear however, that not all ODA supported programs administered by the GFIs have been implemented as quickly and smoothly as expected. An assessment should be made as to whether problems in relending of ODA funds to LGUs by the GFIs are a result of the design of the lending facilities themselves, inadequate capacity on the part of the GFIs themselves or the LGU borrowers, or unexpected changes in macroeconomic variables such as low domestic interest rates..

Many LGUs particularly the lower tier LGUs have not availed themselves of loans either from the MDFO or the GFIs. It is not exactly clear what the reasons for this are. The reasons could relate to lack of ability to prepare projects, lack of creditworthiness, poor management of existing resources, etc. It would be useful to conduct a random survey of selected LGUs from the bottom two tiers, to determine what the reasons are and to develop a response. This would better allow a firmer determination as to whether MDFO should retain some retail lending capacity for the lowest income, poorest LGUs.

4. Partial LGU and Private Sector Ownership of MDFO

If MDFO is transferred out of DOF and corporatized, the question of ownership of MDFO could also be opened up. In the Nordic countries, it is common for municipal finance institutions to be at least partially owned by local governments. The Nordic municipal finance institutions operate under a "credit union" style of management. The advantage is that it increases local government participation and responsibility. Peer pressure among local governments to act responsibly is also enhanced. Partial LGU ownership of a corporatized MDFO could be considered in the Philippines. Partial private sector ownership of MDFO may also be considered, using the model of the LGUGC.

C. PROPOSED NEW RESPONSIBILITIES OF THE MDFO

The system of LGU finance in the Philippines could be enhanced by functions that are common in advanced market economies, but which are currently missing in the Philippines that have the effect of increasing competition for LGU lending and increasing access to domestic private capital sources. Depending on whether the MDFO retains its retail lending functions and depending on whether a decision is taken to corporatize the MDFO, the MDFO could assume several of these new functions that would enhance its role as a facilitator of market-based lending to LGUs.

If MDFO is corporatized, several options for new responsibilities are opened up. It could perform any or all of the following new functions:

1) In addition to remaining a channel for on-lending ODA funds to LGUs, begin to leverage ODA funding to help raise domestic private capital;
2) Operate as a second tier provider of funds to government and private banks who would lend to LGUs; or
3) Act as a "bond pooling agency" for LGUs that are not able to float bonds themselves due to size or other reasons.

If the MDFO gives up its retail lending functions in favor of a GFI, then as a government institution it could then concentrate on the following:

4) Administer matching grants to LGUs, as part of the Government's Loan-Grant-Equity mix program (being even-handed among different LGU lending institutions); and/or
5) Provide policy-based loans and grants to LGUs to improve policies on resource mobilization and expenditure management.

In addition, since the MDF Policy Governing Board will continue to guide and oversee the implementation of the LGU Financing Framework, it may direct the MDFO to prepare an annual report on progress made and outstanding issues

1. Leveraging ODA to Raise Domestic Capital

Currently MDFO obtains all its funding from international loans. Given that there is a need to increase domestic private funding of LGU investments, a corporatized MDFO could at some point play a helpful role by floating domestic bonds that would be used for local government lending. Multilaterals could be asked to help design such schemes and to use part of their funding to support a domestic bond flotation. This would lesson the Government's dependence on foreign borrowing and further increase the level of private capital into the LGU market in accordance with the LGU Financing Framework.

The Tamil Nadu Fund in India has been able to successfully tap private domestic financing and co-financing for its LGU sub-projects.

2. Second Tier Financing

The MDFO can play a more proactive role in removing the bottlenecks that deter private bank lending to LGUs and in improving LGUs' access to private capital. One way to do this would be for MDFO to become a wholesaler of funds for GFIs and, eventually, private financial institutions (PFIs) desiring to lend to LGUs. It could initially employ funds from official development institutions to play this role, but any second tier program should be structured from the beginning in a way that could also utilize foreign and domestic private capital markets.

Successful examples of second tier institutions can be found not only in the developed countries but also in the developing world. FINDETER in Colombia has been successful in introducing commercial banks to local government lending through a rediscounting mechanism. Colombia has reached the point where many private commercial banks in the country now lend to local governments without reliance on FINDETER. The Czech Republic also has a similar institution.

The MDFO could play the role of a second tier institution by

- acting as a wholesale provider of ODA and private funds to government and private banks by providing these institutions with a line of credit or by providing them with a long term loan; or
- rediscounting loans after they are made.

The first approach could be similar to that employed in the JBIC Environmental Services Support Project in which DBP on-lends JBIC funds to private banks. The difference would be that the private bank that receives the funds in this case would on-lend to LGUs rather than to private companies. Alternately, MDFO could rediscount loans originated by the private institutions after they are made. Utilizing the private banks as primary lenders of long-term ODA funds would have the advantage of serving to introduce the private banks to the LGU market and to provide them with an opportunity to develop relationships with LGU clients. Increasing private bank lending is a central objective of the *LGU Financing Framework*. The requirement that the private banks conduct their own appraisal and be free to make their own credit decisions and bear all risks should be the guiding principle in any agreement between MDFO/DOF and the private banks. The private banks could also be asked to supplement MDFO funds with their own internally generated funds e.g. they could be asked to use their own internally generated funds for 20 to 25 percent of any loan amount. The use of ODA funds should permit sub-loans by private banks to LGUs at longer tenor than would be possible with only the private banks' own generated funds. Longer tenor would permit a closer match with the needs of various types of infrastructure projects.

Rediscounting has attributes that would readily lead to securitization. MDFO could package its contractual revenue flows from private commercial banks, securitize them, and use these flows to raise additional money in the domestic capital markets. Because these loans might be of somewhat longer tenor than standard commercial loans due to ODA enhancement, securitization could also introduce a longer term fixed income security to the domestic capital market. This would assist the government's goal of capital market deepening.

The track record of LGU loans that have been made by GFIs and the MDF has been almost perfect since the implementation of the 1991 Local Government Code. However, the private banks do not have a depository relationship with LGUs and are not very familiar with LGUs or with the experience of the GFIs with LGU debt. As noted above, private banks have been reluctant to lend to LGUs because of perceived political risks. Discussions should be initiated with the LGUGC to see whether it may be feasible for the private banks to utilize the guarantee of the LGUGC, which would provide cover against political as well as other risks. If this is a realistic possibility, an LGUGC guarantee may provide enough additional comfort to encourage private banks at the margin to begin to consider the LGU market, with wholesale funds provided in part by the MDFO.

It is likely that initially, private banks would be interested primarily in upper tier LGUs, but this is entirely consistent with the graduation concept in the LGU Financing Framework

This option almost certainly would also require a depository relationship between LGUs and accredited private banks. Opening discussions with private banks on this topic is timely and actions to remove the policy bottlenecks to private bank lending need to be taken.

It would be best if the institution responsible for wholesaling were not also responsible for retailing. Thus if MDFO continued direct lending to LGUs, there could be conflict with its picking up the responsibility for wholesaling. A minimum management condition for effectiveness would be that the wholesaling institution be corporatized. Private financial institutions in the Philippines have also indicated that a second tier institution is more likely to be successful and accepted by the market if it were privately managed. The private banks are wary of political interference and believe that the dependability and efficiency of transactions are critical. They believe that efficiency and credibility of a wholesaling institution would be enhanced if the institution were privately managed, perhaps along the lines of LGUGC or through a management contract.

3. Bond Pooling

During the past twenty years, many developed countries have realized that there is a niche for institutions to issue bonds on behalf of small and medium sized local governments that otherwise would find it too costly or who would not have the credibility in the market to issue a bond on their own. The Philippines may be close to the point where there would be market acceptance of a pooled bond product of municipal governments. Bond pooling would benefit a wide range of local governments, but would especially benefit the smaller, less well-known local governments who could not issue bonds on their own. Under this scheme, the bond pool institution would review borrowing proposals from LGUs during a fixed period of time, say three to six months. It would then issue a bond in its own name, in an amount matched to the LGU needs. The bond pool would be backed by the promised revenue flows from loans made to the approved diverse group of LGU borrowers. Based on international experience, to gain market acceptance, the bond pooling institution would need a reserve fund at least equal to one year's debt service, and a pledge of IRA receipts from LGUs. Acceptance by the market would depend on many factors including the financial strength of the bond pooling institution and the strength of its management. A back up guarantee by a multilateral or bilateral development agency might provide further support to initial offerings. The LGUGC may also be interested in providing guarantee coverage to a bond bank issue.

Experience indicates that management of the bond pooling function should be under a corporate style structure, even if ownership remains with government. While bond pooling is inherently simpler than retail banking, such institutions do need make judgments about which local governments are sufficiently creditworthy to be included in the bond pool and they need to take decisions and manage risks in a business-like manner. Some bond banks provide local governments with other value added services such as liquidity management, and equipment leasing, which require additional management skills. If the MDFO picked up bond bank responsibility, consideration would have to be given to having MDFO managed independently under a corporate style management contract.

Bond pooling should not be the responsibility of a bank that is also already responsible for direct retail lending to LGUs. To preserve competition and choice by LGUs, bond pooling and retail banking should be considered to be competing sources of funds for LGUs. An institution that handled both (whether MDFO or a GFI) might tend to steer an LGU client to the option most profitable to the institution. LGUs should have a choice of competing sources.

An in depth study of the market demand, feasibility and institutional and financial arrangements for bond pooling is needed.

4. Providing Matching Grants, but with a Level Playing Field

As noted in Section I, the ICC has authorized a loan–grant matching scheme to provide specific subsidies to LGUs based on the LGU income class and type of project. However, currently, matching grants are provided ***only*** for projects being administered by the MDFO. It is recommended that the policy on matching grants be made more consistent not only across projects or programs but also across funding or loan sources. Thus, an LGU undertaking a particular type of project should be eligible for a matching grant, based on the merits of the project, regardless of whether it takes out a loan from the MDFO or a GFI, or a PFI for that matter.

If the MDFO were not corporatized, it likely would retain its responsibility for administration of the loan-grant equity mix. The MDFO can administer the matching grants for eligible projects but should consider doing it no matter which lending institution made the loan. This would have the advantage of leveling the playing field among institutions that lend to LGUs and increasing the range of choices available to LGUs. Under the proposed scheme, a loan that any GFI or PFI would make to an LGU for a project eligible for cost sharing could be matched with an MDFO grant. Even an LGU that wished to float a bond for an eligible project could, in principle, also benefit from an MDFO grant.

Best practice internationally is for retail lending and grant making to local governments to be carried out by separate institutions. If in the future, MDFO gives up its responsibility for retail lending to LGUs, MDFO would be a good candidate to continue to administer grants under the ICC framework for Loan-Grant matching schemes. Some have expressed the concern that dividing loan making and grant giving between two different institutions would lead to delays and inefficiencies in project financing when a project requires both a grant and a loan. However, there may be no other alternative but to develop such a mechanism that will be able to deliver the required results with as much efficiency and equity as possible. To avoid problems and delays of this type in administering grants, it is important that the rules for grant allocation be spelled out very clearly. LGUs and lenders must both understand the rules and have confidence in their administration. Decisions on grants made by MDFO should be almost automatic, according to strict and specific eligibility formula.

5. Providing Policy-based Loans and Grants

The MDFO, if it is not corporatized, but remains part of government, could also have a special mandate to support LGU policy reform by making policy-based loans and grants. There is a great deal of capacity building and reform required at the LGU level. The World Bank's OED evaluation of the MDF cited the positive impact of the MDF on municipal capacity building. This could be built upon and expanded. The MDFO could offer program loans and grants to LGUs in return for major policy reform. The type of reforms LGUs can undertake include significant increases in the percentage of total revenue accounted for by own revenue sources; improved public information covering financial data, budgets, procurement, and performance indicators; improved staff skills and staff hiring practices; implementation of modern planning and programming of investments; and formulation of participative local development plans and strategies. A question to be answered is whether demand exists on the part of LGUs for such lending. There is a feeling that many local chief executives who are concerned about explaining debt payments to their council may not be willing to borrow for policy reform. This can be somewhat addressed by including a specific capital investment project in the package, so that there was an element of learning by doing. If there was also significant grant element to the program, additional LGUs would be interested. Including a project and a grant element in the package could therefore be considered to provide an incentive to LGUs who would otherwise be reluctant to borrow for policy or structural reforms only.

A concern has been expressed that many small, poor local governments are not availing of loans. Some have suggested that this justifies continued MDFO lending to poor LGUs, because MDFO could make loans to low income LGUs that GFIs would not make. However, it would be problematic if MDFO began to make loans with poor credit quality and found its default rate going up. This would create a bad precedent, go counter to the need to develop a credit culture among LGUs, and foster a poor image of LGU lending that could set back the introduction of private lending. Thus the creditworthiness criteria used by the MDFO should be the same as that of the GFIs.

To the extent that the investment needs of poor LGUs are not being met with the subsidies currently available to them through IRA and through the Loan-Grant-Equity mix program, it is strongly recommended that a survey of poor LGUs be undertaken to determine the reasons why they are not borrowing. If it is determined that further assistance is warranted, then, rather than distort lending criteria, it may be better to have a very small and targeted special grant program for these cases. It is likely and preferable that any such grant be tied to policy reforms (see above). This could be confirmed by the suggested survey. It should be noted that with the formulas adopted in the current matching grant program, many types of projects of lower tier LGUs are already highly subsidized. This should permit any special capital grant program to be of fairly modest size and related to reform or capacity building efforts. A more detailed analysis should be undertaken to define the specific eligibility criteria and conditions under which a capital grant subsidy would be made available to a lower tier LGU and to define circumstances when a loan might be made instead of a grant. The grant should be time-bound and performance-based in line with the graduation policy.

D. ADVANCING THE IMPLEMENTATION OF LOGOFIND

For the LOGOFIND project, the World Bank provided a US $100 million loan to the government to be channeled through MDFO for technical assistance (TA) and loans and matching grants to LGUs. Because of delays in implementation, US $40 million of the loan has been cancelled. To speed up the utilization of the remaining balance, the following actions are recommended for consideration by the PGB and MDFO:

1. Activate fund for feasibility studies and assist LGUs engage consultants

Despite the large backlog of urgent investment needs at the LGU level, a major constraint to the full allocation of LOGOFIND funds has been a limited pipeline of well-prepared project feasibility studies from LGUs. It is recommended that the MDFO assist LGUs in having project feasibility studies prepared. Steps should be taken to activate the existing fund for feasibility studies and make it attractive for LGUs to avail of.

LGUs could still be asked to borrow from MDFO for the cost of the feasibility studies. LGUs who decide to proceed with the project under LOGOFIND can have loan repayment for the feasibility study rolled into the repayment for the investment project. Alternatively, some amount of grant support might be considered, particularly for any training component to be included. There are medium term benefits to having some of the LGU staff trained in the making of feasibility studies so that they will not have to borrow again for future projects. This training component can be financed under the technical assistance component for capacity building.

Since many LGUs are not experienced in hiring consultants, the MDFO can assist by pre-qualifying consultants. A bidding process can be used for pre-qualification with the understanding that the actual engagement of the selected consultants would only occur when an LGU decides to proceed. This would be consistent with the principle that sub-project feasibility studies be "demand driven". It would also limit costs and ensure that work was done only when an LGU was prepared to move forward. Given the nature of the work it would be expected that most consultants would be local. Several teams of consultants can be pre-qualified and made available to LGUs in different regions on a demand basis. Having MDFO pre-qualify the consultants would likely lead to higher quality feasibility studies since consultants would be working across multiple LGUs and feasibility studies would be developed in a consistent manner using common standards.

2. Activate and open up TA components on capacity building and resource mobilization to prepare more LGUs for sub-project implementation

In addition to the hiring of consultants to assist LGUs in the preparation of feasibility studies, additional steps should be taken to make more LGUs ready to implement sub-projects. The TA components of LOGOFIND for LGU training and capacity building and for LGU resource mobilization should be activated as soon as possible and utilize the expertise that has been built up through LOGOFIND's predecessor projects, for example, in the Local Government Academy of the DILG. The TA should also be opened up to LGUs which are interested in undertaking a sub-project but which have not yet proposed one or had one approved by LOGOFIND. The TA components were made as large as they are to provide more LGUs with the financial and managerial capacity to undertake sub-projects. While technical assistance is provided to LGUs implementing sub-projects under LOGOFIND, building up the pipeline of LGUs that would propose sub-projects to LOGOFIND is also one major objective and the key to developing a robust pipeline of sub-projects for future funding.

The sharing of responsibilities for general capacity building and local development planning should be worked out with the Department of Interior and Local Governments and its Local Government Academy and the NEDA, respectively, and with concerned national government agencies such as the Department of Public Works and Highways and Department of Environment and Natural Resources for sector-specific technical assistance

V. SUMMARY OF MAIN RECOMMENDATIONS

The challenge of improving municipal finance is at heart a challenge of good municipal management. Rating agencies and private investors, whether domestic or foreign, consider good municipal management to be one of the first requirements for a positive credit decision. The *LGU Financing Framework* therefore will affect LGU management as well as finance. Because of this, the timely implementation of the *LGU Financing Framework* will contribute greatly to reaping the benefits envisioned by the 1991 Local Government Code.

The *LGU Financing Framework* basically embodies forward-looking objectives, principles and strategies of sound local government finance that are still very much valid today. The vision of the *Framework* is anchored on two premises:

> *"First, LGUs have varying levels and records of creditworthiness and bankability. Second, their financing needs are huge.*
>
> *Therefore, the private sector (BOT investors, bondholders, commercial banks), the GFIs and MDF all have a role to play in meeting LGU financing needs.*
>
> *The ultimate objective is to graduate LGUs to private sources of capital which are vast and promising, but remain largely untapped."*

What is needed is to complete the phase one reorganization and strengthening of the MDFO, to carefully examine the options for the second phase restructuring of the MDFO and to make appropriate decisions and preparations. The first step is the development of greater understanding of the objectives and strategies of the *Framework* by all sectors concerned and consensus on courses of action to be taken by individual agencies and institutions. Toward this end, multi-sectoral consultations and discussions among national government agencies, various levels of local governments, government and private financial institutions, prospective BOT proponents and LGU bond investors, and ODA sources would be very useful if not imperative.

A. PREPARATION OF AN IMPLEMENTATION PLAN FOR LGU FINANCING FRAMEWORK

Only after such consultations can a detailed implementation plan for moving ahead on the entire *LGU Financing Frame-work* be prepared. The roles and responsibilities of each party need to be spelled out along with an agreed set of actions and a timetable for each party. The implementation plan needs to be realistically based on resources available-- both human and financial. It is recommended that the MDFO- PGB host these consultations and appoint an inter-agency committee to prepare an Implementation Plan.

B. FIVE KEY RECOMMENDATIONS TO IMPLEMENT THE LGU FINANCING FRAMEWORK:

1. **Complete the Phase-One Reorganization and Strengthening of the MDFO.** For the MDFO to carry out its mandated functions more efficiently and effectively, the following measures are recommended to be undertaken as soon as possible:

   a. Have regular plantilla positions approved for all budgeting, accounting and internal auditing functions and project appraisal teams;

   b. Conduct needs assessment and intensive training of all personnel in LGU finances, credit processes, project preparation and appraisal, and marketing and communication skills;

   c. Speed up the computerization of existing loan and grant records and setting up of a management information system for new projects and programs;

   d. Streamline loan and grant disbursement procedures; and

   e. Institute formal performance and financial auditing procedures.

2. **Implement Comprehensive LGU Information System**. The BLGF, in coordination with the Department of Budget and management (DBM) and the Commission on Audit (COA), should give priority to the development and implementation of comprehensive and consistent information systems that will make available on a timely basis important financial information about LGUs including the following:

   a. Approved budgets and programs of expenditure for the current year and immediately preceding years;
   b. Sources of income during the current year and immediately preceding years, income projections and assumptions for the next few years, and classification of income into regular and special; and
   c. Relevant information on all grants received and existing loans and other obligations and projected debt servicing.

3. **Take Steps to Level the Playing Field between Private Banks and GFIs**. A level playing field is necessary to encourage the eventual gradual introduction of private bank lending to LGUs. The DOF, in consultation with the concerned government agencies, should take the necessary measures to make it possible for:

   a. Selected private banks to become depositary banks for LGUs;
   b. Extension of the IRA intercept to private banks that have become depositary banks for LGUs; and
   c. LGUs to borrow from any source including private banks, and still have eligible projects benefit from the government's Loan-Grant-Equity Matching scheme in line with guidelines for that scheme.

4. **Support Increase in Capitalization of LGUGC**. The DOF should support the LGUGC in discussions on increases in its capitalization with the private sector arms of multilateral development agencies (ADB, IFC, JBIC) or any bilateral donors that may be interested.

5. **Prepare for Second Phase Restructuring of MDFO**. During the coming months, the DOF and MDFO can do the spade work for the implementation of the second phase of the MDFO restructuring which can involve the corporatization of MDFO, or the transfer or assignment of one or more of the present functions of the MDFO.

   Several options based on principles of best international practice can be considered for the second phase. The principles of international practice suggest a) that municipal lending institutions should have *corporate style management* if not privatized management; b) that *grants* to local governments and normal *retail loans* should be handled by separate institutions; c) that *retail* lending and *wholesale* lending should be done separately; and d) that there should be competition among institutions for local government lending

   Option 1:
   If the MDFO shifts its current routine retail lending to GFIs and eventually PFIs, then the MDFO could remain in the DOF and continue to be the government institution responsible for matching grants and technical assistance to LGUs. It could also take responsibility for policy-based loans and grants to LGUs willing to undertake significant reforms. In this case, DOF should assess the market need for and institutional arrangements appropriate for a new corporate style or private sector body that would take on responsibility for a) bond pooling on behalf of LGUs or b) wholesale lending to private banks to encourage private bank lending to LGUs.

   Option 2:
   If MDFO retains its current function of retail lending to low income LGUs for routine borrowing needs, then MDFO should be corporatized. If direct conversion of MDFO into a new GFI is not considered feasible in the near term because of the need for new legislation, one way to achieve corporatization may be to have the MDFO managed under a management contract by a private or non-profit corporation. Another, perhaps simpler, way to achieve corporatization would be to transfer the MDFO to a specially created subsidiary of an existing GFI. A necessary condition of such a transfer should be that the management of the subsidiary should be independent of the day-to-day management of the mainline operations of the GFI if that GFI were itself already making loans to LGUs. This is to avoid conflicts of interest between the subsidiary and the mainline lending operations of the GFI. The various means of corporatizing the MDFO without requiring new legislation would need to be studied in greater detail to ensure consistency with existing legislation, principally P.D.1914. Due consideration would also have to be given to which existing or new institutions would carry out the grant-giving functions presently exercised by MDFO and the bond pooling function that has been noted to be an essential component of a mature municipal finance system.

   Option 3:

An alternative vision for a corporatized MDFO would be for it to act as a bond bank or a second tier institution that would lend on wholesale terms to government or private banks for LGU lending. ODA funding could also be used to help support and implement an approach involving bondbanking or second tier lending. The responsibility for LGU grants and policy-based loans to LGUs in this case could remain with the DOF. In all cases, an assessment should be made of how the corporatized MDFO could use access to ODA funds to help it to eventually become at least partially self-standing and to begin to tap the domestic capital markets.

If the MDFO is to be corporatized, the legal issues associated with changing its ownership structure should be explored, whether or not it is transferred to a subsidiary of a GFI. In principle, a number of ownership options exist. It could remain entirely government-owned or some private investment could be sought along the lines of the LGUGC. It would even be possible to allow some ownership in a corporatized MDFO to be held by the LGUs themselves. Partial ownership of municipal lending institutions by the borrowing LGUs is common in the Nordic countries of Europe where communal banks have a large part of the local government finance market. This would require that LGUs or an LGU association be allowed to buy shares.

In summary, selection and implementation of the best alternative would be facilitated by the following steps:

a. Assess the desirability and legal and financial viability of unbundling the grant making and loan making functions of the MDFO;
b. Assess the market need and readiness for bond pooling on behalf of LGUs and for wholesale lending to private banks to encourage private bank lending to LGUs;
c. Consider various options for corporatizing MDFO, particularly those not requiring new legislation;
d. Consider various ways in which a corporatized MDFO could leverage ODA funds to raise domestic capital;
e. Explore the possibility of opening up the ownership of the MDFO to LGUs or the private sector; and
f. Assign specific MDFO personnel to coordinate work on the above as well as on removing the bottlenecks to private sector lending to LGUs.

C. SUPPLEMENTAL RECOMMENDATIONS TO IMPLEMENT THE FRAMEWORK

- **Prepare Annual Report on Performance of Outstanding LGU debt**. In the absence of a private rating agency, it is recommended that the BLGF publish a special annual report on the financial condition of local governments that have already issued bonds. This report should cover the repayment experience to date–with LGU bonds and any changes in the financial position of an LGU that would affect the ability of the issuing LGU to service its debt. The report might also include an independent audit of the performance and status of the LGU portfolio of the GFIs to provide further information to potential investors and bankers who are not familiar with LGU securities and the performance of LGU debt. Consideration should be given to involve the Bankers

Association of the Philippines in drawing up the terms of reference and in the selection of a reputable consulting or accounting firm to carry out the first annual review.

- **Use ODA to Support the Development of the Domestic LGU Credit Market**. Multilateral and bilateral development agencies should be encouraged to employ lending modalities (e.g. backup guarantees, measures to lengthen maturities of private debt, etc) that utilize ODA funds to help local institutions leverage domestic private sector funding to LGUs, where this is feasible, rather than utilizing these ODA funds only for direct on-lending.

- **Support Secondary Trading Facility for Bonds**. The recent initiative of the Bankers Association of the Philippines to create a secondary trading facility for fixed income securities should be reviewed by DOF to determine what regulations are needed to support this initiative.

- **Coordinate Government Approaches to BOTs for LGUs**. Regular consultation meetings should be held among the CCPSP, NEDA, DILG-LGA, DOF-BLGF, MDFO, the GFIs, and LGU representatives to review actual experiences with BOTs and adopt measures to make BOTs an attractive financing alternative for LGUs as well as viable propositions for BOT proponents. Sustained marketing and advocacy campaigns can also be undertaken to help LGUs fully understand the advantages and disadvantages of BOT and other similar schemes. Regulatory and policy issues should be discussed and resolved as soon as possible.
- **Maintain Market Based Lending Terms for MDFO and GFI Lending**. The GFI and MDFO policy of lending to LGUs at market terms should be maintained in order to avoid discouraging private funding through private banks or bond issues. Care should be taken to ensure that rates adjust to sustainable changes in market conditions, with due consideration of the cost of the funds being onlent.

- **Expand LGU Access to Funds for Local Development Planning and Project Feasibility Studies**. Because one of the key constraints to effective lending is the absence of well-chosen and well-prepared projects, NEDA, DILG and MDFO should step up their efforts to inform LGUs about the existing facilities available and prepare new facilities and modalities.

- **Undertake information dissemination and educational campaigns for LGUs to learn about various financing options and their proper utilization.** These include BOT arrangements, bond flotations, and loans from the MDFO and GFIs.

- **Provide Incentives for LGUs to Increase Own Revenues**. LGUs should be given greater incentives to increase own source revenue. An adjustment to the IRA allotment formula should be considered that would result in a higher IRA when an LGU demonstrates a relatively high degree of effort in raising its own resources.

D. FURTHER STUDIES

Additional work is needed to:

- Make an inventory of all budgetary resources going to LGUs, determine the future budgetary requirements of all ongoing projects through which the national government provides loans or grants to LGUs, and determine from a macroeconomic point of view the long-term sustainable amount available from future budgets for such expenditures.

- Review the cost-sharing formula (the Loan-Grant-Equity mix scheme) for all existing and pipeline projects and rationalize this with a view to having the scheme uniformly applied to all projects, whether foreign-assisted or locally-funded and ensuring that subsidies are affordable and sustainable for the national government. Other devolved sectors not included in the initial guidelines should also be considered. The desirability and legal and financial viability of unbundling the grant making and loan making functions of MDFO should be assessed with the end in view of making all lending institutions eligible to participate in the Government's Loan-Grant-Equity mix scheme

- Conduct a survey of LGUs to document and learn from their experiences with the various sources of financing such as BOTs, bond flotations, borrowings from the MDFO and GFIs, and to identify the obstacles to their availment of these financing alternatives. More particularly, for LGUs in the bottom three tiers, it would be necessary to determine why only a small percentage have availed of loans. This would allow a firmer determination as to whether MDFO should retain some retail lending capacity for the lowest income, poorest LGUs.

- Prepare an operations manual for policy-based loans and grants by MDFO and define the specific eligibility criteria and conditions under which a capital grant subsidy would be made available to the bottom tier LGUs.

- Review the terms and conditions and re-lending rates of loans to LGUs from various sources and recommend changes to promote consistency wherever necessary and improve the balance between competing objectives.

- Study the market demand, timing, institutional arrangements, capital structure, and legal steps for a second tier institution to support the entry of private commercial institutions into the local government market, and for bond pooling.

E. RECOMMENDATIONS TO ADVANCE THE IMPLEMENTATION OF LOGOFIND

1. Activate fund for feasibility studies and assist LGUs engage consultants.

Steps should be taken to activate the existing fund for feasibility studies and make it attractive for LGUs to avail of. While LGUs would still be asked to borrow for the cost of the feasibility studies, some amount of grant support might be considered, particularly for any training component to be included. There are medium term benefits to having some of the LGU staff trained in the making of feasibility studies so that they will not have to borrow again for future projects.

Since many LGUs are not experienced in hiring consultants, the MDFO can assist by pre-qualifying consultants. A bidding process can be used for pre-qualification with the understanding that the actual engagement of the selected consultants would only occur when an LGU decides to proceed. Several teams of consultants can be pre-qualified and made available to LGUs in different regions on a demand basis. Having MDFO pre-qualify the consultants would likely lead to higher quality feasibility studies since consultants would be working across multiple LGUs and feasibility studies would be developed in a consistent manner using common standards.

2. Activate and open up TA components on capacity building and resource mobilization to prepare more LGUs for sub-project implementation

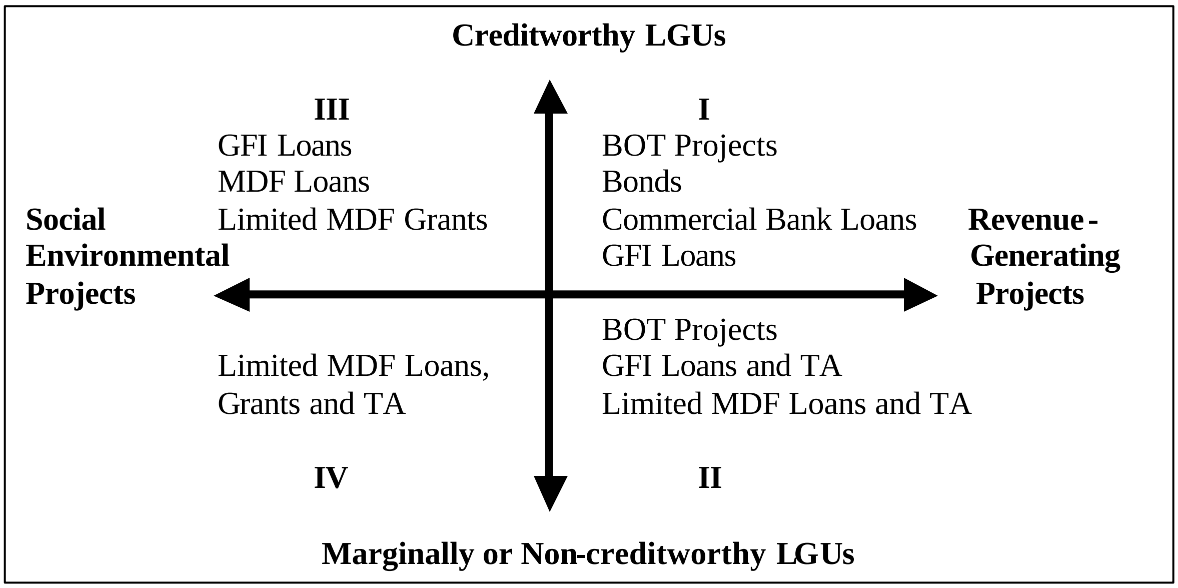
The TA components of LOGOFIND for LGU training and capacity building and for LGU resource mobilization should be activated as soon as possible and utilize the expertise that has been built up through LOGOFIND's predecessor projects, for example, in the Local Government Academy of the DILG. The TA should also be opened up to LGUs which are interested in undertaking a sub-project but which have not yet proposed one or had one approved by LOGOFIND. While technical assistance is provided to LGUs implementing sub-projects under LOGOFIND, building up the pipeline of LGUs that would propose sub-projects to LOGOFIND is also important.

The sharing of responsibilities for general capacity building and local development planning should be worked out with the Department of Interior and Local Governments and its Local Government Academy and the NEDA, respectively, and with concerned national government agencies such as the Department of Public Works and Highways and Department of Environment and Natural Resources for sector-specific technical assistance.

Annex I-A

Credit Policy Framework for LGUs

The LGU Financing Framework clusters LGUs into four groups based on their creditworthiness and the types of projects to be undertaken. In so doing, the Framework seeks to rationalize the use of credit and grant facilities for the financing of different types of LGU projects.



On the vertical axis, LGUs are classified according to creditworthiness, with the most creditworthy on the top and the marginally or non-creditworthy at the lower end. On the horizontal axis, revenue-generating projects are on the right side and projects with social and/or environmental objectives, usually with long gestation, are on the left side.

The first quadrant shows that *creditworthy LGUs with revenue-generating projects* can get financing from GFIs (from their own funds), private commercial banks, the bond market or enter into BOT arrangements. The rationale is clear: revenue-generating projects of creditworthy LGUs can be funded mostly from private sources of capital.

The second quadrant shows that *marginally or non-creditworthy LGUs with revenue-generating projects* could have funding from BOT arrangements, GFI loans with technical assistance, and limited MDF loans and technical assistance. The key element here is the revenue-generating nature of the project. With viable and sustainable projects, the LGU could enter into BOT arrangements or obtain GFI or MDF loans with supplementary technical assistance grants to improve creditworthiness. The LGUs may have the financial resources but lack the project management capability to be truly creditworthy.

In the third quadrant, *creditworthy LGUs undertaking social/environment projects* whose returns are low or long in coming could be allowed to tap long-term, lower-cost ODA funds through loans from the GFIs or MDF. They may also be eligible for limited grants from MDF.

In the fourth quadrant, the *marginally or non-creditworthy LGUs with social-environmental projects* could be assisted by loans and grants from the MDF, in accordance with the approved policy of the NEDA-ICC, and technical assistance.

Source: LGU Financing of Basic Services and Infrastructure Projects:
A New Vision and Policy Framework
Department of Finance, December 1996

Annex I-B

LGU Bonds Guaranteed by LGUGC

Issuer	Project	Trustee	Amount (million pesos)	Term
City of Urdaneta	Abbattoir	Philippine Nat'l Bank	P25 million	5 yrs; interest payable every 6 months; principal on maturity
Province of Aklan	Jetty Port & Terminal Building	Land Bank of Philippines	P40 million	7 yrs; interest payable every 6 months; principal on maturity
City of Puerto Princesa	Low Cost Housing	Philippine Nat'l Bank	P320 million	7 yrs; interest payable every 6 months; principal amortization for 5 yrs commencing on 3rd year
City of Tagaytay	Tagaytay City Convention Center	Philippine Nat'l Bank	P220 million	7 yrs; interest payable every 6 months
City of Caloocan	City Hall Commercial Complex	Philippine Nat'l Bank	P225 million	7 yrs; interest payable every 6 months; equal principal amortization for 6 years starting on 2nd year
City of Caloocan	Caloocan City Hospital	Philippine Nat'l Bank	P215 million	7 yrs; interest payable every 6 months; equal principal amortization for 6 years starting on 2nd year
City of Caloocan	Caloocan City Public Market	Philippine Nat'l Bank	P180 million	7 yrs; interest payable every 6 months; equal principal amortization for 6 years starting on 2nd year
City of Iloilo	Government Housing Project	Philippine Nat'l Bank	P130 million	3 yrs; interest payable every 6 months; equal annual principal amortization of P43.3 million

Annex I-C

History of Loans to LGUs					
Year	**New LGU loans approved (number)**	**Total peso value of new loans (millions)**	**% of new loans to 3-6 tier LGU's during year (%)**	**% of new loans from ODA sources (%)**	**Total peso value of outstanding LGU loans (releases less collections) (billions)**
Land Bank (LBP)					
2000	94	4,375	N/A	0.7	11.86
1999	84	4,715	73	12.5	7.54
1998	50	1,583	58	0	4.35
1997	36	2,853	44	0	3.77
1996	41	6,374	76	63.5	2.36
1995	114	4,693	34	0	1.02
Development Bank of Philippines (DBP)					
2000	55	347	N/A	100	1.73
1999	37	173	N/A	100	0.81
1998	23	91	N/A	100	0.41
Municipal Development Fund Office (MDFO)					
2000	55	405	28	100	N/A
1999	33	270	37	100	N/A
1998	33	375	19	100	N/A
1997	19	248	32	100	N/A
1996	20	219	1	100	N/A
1995	19	254	0	100	N/A
N/A = Not Available					

Sources: LBP, DBP, MDFO

ANNEX II-A
Lending Facilities for Local Government Units
As of end December 2001

Program/Project Title	Funding Institution	Implementing Agency	Description	Duration	Loan Amount (In Million Pesos)	Terms and Conditions of Funding Institution	Location	Re-Lending Terms and Conditions	Cost-Sharing Arrangements	Status/Remarks
I. Through Government Financial Institutions										
A. *Land Bank of The Philippines*										
1 Water Districts Development Project - Sewerage, Sanitation, Drainage (WDDP)	WB	LBP, Local Water Utilities Administration (LWUA), MWSS, DOF, LGUs	The project intends to provide subloans to first to third class LGUs to expand sanitation services in project areas nationwide and develop Public Performance Audit Plans to strengthen the capacity of the LGUs to contract out the operation of water supply and sanitation systems. Project components to be funded include: a. Trunk (capital) investment in sewerage, sanitation, drainage and wastewater treatment infrastructure. Trunk investment will finance feasibility study and detailed design, construction and rehabilitation of sewerage main drains, wastewater treatment facilities; b. Feeder investments in barangays requiring immediate environmental and sanitation investment programs such as water supply, sanitation, microdrains and solid waste collection and disposal.	1999-2004	1,452.00 (Forex $36.3 m)	6.53% (Interest Rate) 0.25% (Commitment Fee) 17 years (Maturity period) 3 years (Grace period)	Nationwide (outside of Metro Manila). 6 Participating LGUs are the following: San Fernando City Panabo City Palawan Cabanatuan City Lapu-lapu City (approved by LBP) Olongapo City (approved by LBP)	Interest rate is 14% per annum fixed. Commitment fee of 0.25% per annum to be charged on the undis-bursed LGU loan. Pre-termination fee of 2% on the outstanding balance shall be imposed.	LP/LBP - 90% and LGU - 10% of total project cost.	Utilization rate still low due to political issues at the local level such as changes in leadership, lack of Sanggunian resolution, among other things.
2 LGU Support Credit Program (LGUSCP)	JBIC	Land Bank of the Philippines (LBP)	The program provides financing to selected provinces, cities and municipalities to construct approved urban sector infrastructure components such as water supply, drainage, flood control, sewerage and solid waste systems, forestry, and other environmental projects. It aims to augment sources of development funds for LGUs through credit assistance. Eligible projects are: a. Sub-project preparation loan - preparation of feasibility study; and, b. Sub-project investment loan such as: - Low cost housing project - mass construction of high rise building (maximum 4 storeys) or row house type with a minimum floor area of 25-36 sqm. and dwelling unit cost of around P150,000-300,000; - Health sector project - construction of public hospital or rural or barangay health centers and purchase of medical equipment; - Water system project - improvement/construction of the LGU's water distribution system; - Flood control and sanitation project - watershed management, and construction of seawalls, dikes, drainage, catch basins, sanitation systems; - Forestry project - community-based forestry management including forestation and reforestation activities; - Waste disposal project - construction of solid waste system, sewage treatment system, and water treatment system; and, - Other environmental projects.	1999-2005	2,282.30	1.5% to 2.2% (Interest rate) 30 to 40 years (Maturity period) 10 years (Grace period)	Nationwide in coverage. 4 LGUs have applied: With JBIC concurrence: 1. Municipality of Palompon, Leyte 2. Municipality of Sara, Iloilo 3. Muntinlupa City, Metro Manila For JBIC concurrence: 4. Municipality of Passi, Iloilo	Minimum amount for JBIC loan component per LGU is P5 million while maximum amount is P50 million. Interest rates: Sub-project preparation loan - 12%-12.5% fixed for the term of the loan. Sub-project investment loan - 12% - 14% fixed for the term of the loan. Loan maturity shall be in accordance with the LGU's cash flow, but should not be less than 3 years but not more than 10 to 15 years, inclusive of a maximum of 2 years grace on the principal.	65% of total project cost will be from JBIC funds, 10% from LBP and 25% LGU's equity.	Implementation problems faced by the program include marketing of the facility in view of the elections and the required LGU equity of 25%. To address these, LBP will continue to market the program to elected and re-elected LGUs with a credit rating of Prime to Medium grade. The consultants will also assist the LGUs in project identifi-cation and rapid assessment. Request will also be made to JBIC for the podssible reduction in equity participation from 25% to 10%.
3 LGU Private Infrastructure Project Development Facility	ADB	CCPSP LBP	The project will support regional decentralization and development process by facilitating private financing of infrastructure prokects at the LGU level. The project has two phases: (a) the TA loan which will develop the design of the facility and prepare sample subprojects; and (b) the main facility which is expected to be lodged at a government financial institution. The proposed facility is intended to finance the direct and indirect foreign exchange costs of equipment and services, including civil works. The lending facility is proposed to fund mainly revenue generating projects from $2-10 million or 30% of the funding requirements, whichever is lesser. Projects should be sponsored by the private sector and/or creditworthy LGUs, preferably in the transport, water supply, solid waste disposal, small hydrowater power plants, industrial parks, infrastructure for tourism facilities, public markets and slaughterhouses.	2000-2001	$ 600,000	Variable interest rate based on six month LIBOR for yen plus 0.40% margin 12 yeara (Maturity period) 3 years (Grace period)	Nationwide	Loan Amount: The minimum amount for the ADB loan component per LGU is $15,000 or its peso equivalent; while the maximum amount is $600,000 or its peso equivalent. Repayment is 5 years maximum, inclusive of 1 year grace on the principal and interest. Interest rate is 11% per annum maximum, fixed for the term of the sub-project loans.		TA ongoing. Main credit facility to start in 2003. No disbursements made. To address the concerns of the qualified LGUs, LBP will request ADB for the possible hiring of local consultants, aside from those selected and hired to undertake the feasibility study preparation and to market the project to interested LGUs.
B. *Development Bank of the Philippines*										
4 LGU Urban Water and Sanitation Project (LGU-UWSP)	WB	DILG, Development Bank of the Philippines (DBP) (Executing agencies) LGUs (Implementing	The project provides water and sanitation facilities to LGUs who have not formed a water district in their area. Target clients are in urban centers for small and medium- size municipalities.	1999-2007	1,562.54 (Forex $23.3 m) (Local P156.1 m) ($23.3 million -	6.53% (Interest rate) 0.25% (Commitment fee)	**Batch 1:** Isabela - Aurora Cabatuan Luna Mallig	The DBP sub-project loan shall include costs of feasibility study, technical design and	10% LGU equity and 90% financing through loan. (The required LGU equity ranges from 10% to 25% of total project cost.	Utilization rate is below 20% and The low disbursement rate is due to delays cause by separate bidding processes for FS, detailed design and selection of private operator.

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		agencies-Municipalities)	Phase I has two major components: a. Capital assistance - water supply (construction/		loan amount in original currency)	(Maturity period)	Quezon San Mateo	construction of the water facility. The		The flow of documentation and communications between DBP and
			rehabilitation of water supply systems in 40 small towns); sanitation program (improvements in toilets, on-site facilitation facilities. Funds will be onlent to the LGUs and administered by the water utility.); urban drainage program (financing of investments and consultant services for micro-drainage infras-tructure. b. Technical assistance - Water Utilities Private Sector Participation (WUPSP) Facility (financing for TA in project preparation and conduct of bidding for private sector participation); project development for water supply and sewerage (preparation of F/S and D/E for water supply for about 80 towns) and sewerage development in secondary cities (prepara-tion of F/S and D/E for five cities for future sewerage investments). c. Institutional Capability Building Program - on financial management, contract management, and environmental, sanitation and health aspects.			(Grace period)	Laguna - Magdalena Bukidnon - Kalilangan Lantapan Misamis Occidental - Sapang Dalaga **Batch 2:** Isabela - Delfin Albano Gamu Sta Maria San Mariano San Pablo Santo Tomas Naguilian Kalinga - Pinukpuk Rizal Tabuk Quirino - Aglipay Nagtipunan **Batch 3:** Misamis Oriental - Salay Talisay Jasaan Villanueva Initao Subongcogon Bukidnon - Cabanglasan Kibawe Impasugong Kitaotao Lanao del Norte - Iligan City **Batch 4:** Palawan - Batarasa Cuyo El Nido Magsaysay Roxas Taytay **Batch 5:** Quezon - Buenavista Padre Burgos Lopez Nueva Vizcaya - Bayonbong Dupax del Sur Sta Fe Solano Villa Verde Oriental Mindoro - Baco Bansud Calapan City Gloria San Teodoro Victoria Bohol - Alicia Carmen Mabini Tubigon Ubay Balilihan San Isidro Trinidad Cebu - Malabuyoc Ronda Misamis Occidental - Aloran Baliangao Calamba Lopez Jaena Oroquieta City Panaon Sinacaban Tudela	basic terms of the loan are: 15% per annum interest rate fixed for 15 years; and, 15 years with 3 years grace amortization period.		PMUs has to be improved, as well as the coordination among concerned DBP units to facilitate the disbursement applications. The first condition for WB to process the second APL loan facility has been complied with the constuction and full operationaliza-tion of 9 water systems, these are, Magdalena, Luna, Malig, Quezon, Cabanatuan, San Mateo, Aurora, Lantapan and Kalilangan. On the compliance for the second condition, only 5 LGUs, namely, Magdalena, Kalilanhan, Lantapan, Manolo Fortich and Tabuk, have signed contracts with private operators for devolved operations and management lease contracts. The requirement is for at least 12 LGUs to sign such contracts with private operators.
II. Provided through National Government Agencies										
A. Municipal Development Fund Office										
5 Program for the Essential Municipal Infrastructure, Utilities, Maintenance and Engineering Development (PREMIUMED)	WB	DPWH, LGUs, DOF	The project involves the improvement and construction of various basic infrastructure facilities and acquisition of municipal government equipment.		(Forex$40 m)	No data available.	42 LGUs have availed of the facility in the following provinces of: Bulacan, Batangas, Surigao del Sur, Cebu, Eastern Samar, Sorsogon, Isabela, Albay, Davao del Sur, Eastern Samar,	11%, 20 years to pay, inclusive of 5 years grace period.	No data available.	Completed.

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							Cavite, Pampanga, Camarines Sur, Ilocos Sur, Iloilo, Palawan, La Union, Isabela and Davao del Norte.			
6 Municipal Development Project 2 (MDP 2)	WB	DPWH, LGUs, DOF	The project provides assistance to LGUs in providing basic infrastructure, services and facilities. It also has programs to strengthen financial, technical and managerial capabilities of LGUs.		(Forex $40 m)	No data available.	34 LGUs have availed of the facility in Cavite, Bulacan, Laguna, Metro Manila and Rizal.	14% interest rate per annum, 15 years repayment period inclusive of three years grace period.	90% sub-loan and 10% LGU equity.	Completed.
7 Third Municipal Development Project (MDP 3)	WB	DPWH (Executing Agency) DILG-MTP, LGUs BLGF-DOF,	The project involves (1) the construction and/or rehabilitation of basic infrastructure annd facilities including shore protection, flood control measures, primary drainage systems and primary roads and bridges; (2) provision of equipment and consulting services; (3) implementation of real property tax administration program; (4) establishment of a municipal training program; and (5) conduct of studies. The components included: a. Local component - markets, motorpool, water supply, high schools/health centers, slaughterhouse, municipal pier/wharf, traffic management, solid waste, sanitation, area upgrading, local roads, local drainage and bus terminal; b. National component - roads and bridges, drainages, flood control, shore protection; and, c. Maintenance program.	1993-2001	(Forex/Loan Amount : $68 m)	1/2% of 1% over CQB (Interest rate) 3/4% of 1% of undisbursed balance (Commitment fee) 20 years (Maturity period) 5 years (Grace period)	74 LGUs have availed of the facility in the following provinces: Metro Manila, Pangasinan, Benguet, Kalinga Apayao, Isabela, Cagayan, Nueva Vizcaya, Nueva Ecija, Bataan, Bulacan, Batangas, Quezon, Rizal, Cavite, Mindoro Occidental, Masbate, Camarines Sur, Antique, Aklan, Negros Occidental, Iloilo, Negros Oriental, Cebu, Leyte, Zamboanga del Norte, Zamboanga del Sur, Bukidnon Sultan Kudarat, South Cotabato, Cagayan de Oro, Davao del Norte, Davao del Sur, North Cotabato, Marawi, Surigao del Sur, Agusan del Sur.	11% per annum 15 years repayment period, inclusive of a three-year grace period.	I. Local Government (LG) Component Sub-loan to LGUs - 90% of total project cost of which 70% from WB loan and 30% from MDF; LGUs equity is 10 % of TPC. II. % of LG component to NG Component for Construction and/or reha-bilitation of Basic Infras-tructure NG (DPWH) - 30% of TPC of which 60% is from WB loan and 40% from GOP; LGU (sub-loan + equity) - 70% of TPC. III. % of LG component to NG component for Maintenance Program 1st year - 70% NG and 30% LGU 2nd year - 50% NG and 50% LGU 3rd year - 30% NG and 70% LGU 4th year - 0% NG and 100% LGU	
8 Regional Cities Development Project (RCDP)	WB	DOTC, DPWH, DOF, DILG, NEDA, NHA	The project involves the improvement of physical infrastructure, municipal services and shelter conditions in selected cities.		(Forex $47 m)	No data available.	4 LGUs were beneficiaries: 1. Bacolod City 2. Cagayan de Oro City 3. Davao City 4. Iloilo City	11%, 20 years to pay, inclusive of 5 years grace,	No data available.	Completed projects are: National Housing Authority - for housing loan; Bacolod City - equipment, motor-pool; Cagayan de Oro City - slaughter-house, equipment, motorpool, dump site; Davao City - dumpsite,, bus terminal equipment, drainage, slaughterhouse market, landfill; Iloilo City - equipment, dump site, market and motorpool.
9 Philippine Regional Municipal Development Project (PRMDP)	ADB	DILG (Executing Agency) DPWH, DOF (conduit) LGUs (implementing agencies)	The project aims to enhance the capabilities of the LGUs to deliver services in consultation with the communities. It has two major components: (1) provision of infrastructure and municipal services; and (2) capability building program. The infrastructure subprojects are demand- based. The TA component includes (a) land- related information system; (b) engineering and solid waste management; (c) planning and development; and, (d) human resources development.	1997-2002	1,367.04 (Forex $30 m) (Local P584.04 m)	Variable interest rate 0.75% p.a. (Commitment fee) 25 years (Maturity period) 5 years (Grace period)	Puerto Princesa (Palawan) Tagbilaran (Bohol) General Santos (Cotabato) Iligan (Lanao del Norte)	14% per annum 15 years repayment period, inclusive of a three-year grace period.	68%(sub-loan) - 32% LGU equity for Puerto Princesa. 80% (sub-loan) - 20% LGU equity for Tagbilaran. 53% (sub-loan) - 47% LGU equity for Gen. Santos 21% (sub-loan) - 79% LGU equity for Iligan.	Delays were encountered in view of the late loan effectiveness by two years and other start-up activities due to the national and local elections in 1998. A cancellation of $10 million was made due to the cancellation of Legaspi, Bacolod and Lucena because of financial constraints and new set of priorities of said LGUs. Delays in issuance of ECCs and difficulties in site acquisition were also experienced which affected the implementation of physical infrastructure in some cities. An extension of the disbursement period was likewise approved by

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										ADB to complete the ff: 1) for Puerto Princesa and General Santos Cities, construction of the sanitary landfill components, 2) for Iligan, construction of the bus and jeepney terminal and public market, and 3) for Tagbilaran, procurement of additional solid waste management.
10 Bukidnon Integrated Area Development Project (BIADP)	ADB	Provincial Government of Bukidnon, NIA, DA, DOH, DENR	The project consists of an integrated package of activities aimed at improving the socio-economic status of the poor rural communities in 7 municipalities and 175 rural barangays.Components include: a. Rural Infrastructure - communal irrigation systems farm-to-market roads; b. Community Development Support - community organizing and training activities; agricultural extension services, rural livelihood skills training; c. Social services - health and children services, rural water supply; and, d. Project Management and Institutional Development	1997-2004	933.29 (Forex $15.08 m) (Local P416.31 m) ($18.92 m original loan currency)	6.76% (Interest Rate) 0.75% (Commitment fee) 25 years (Maturity period) 5 years (Grace period)	La Fortuna Maninit Sigmatan Manolo Fortich Baungon	14% per annum 15 years repayment period, inclusive of a three-year grace period.	No data available.	Rural Infrastructure: construction of 2 out of 5 targetted CIS have started in May 2001 and installation of drip equipment for La Fortuna CIS was supposed to have been completed last December 2001. Out of the 70 km farm-to-market roads rehab/upgraded, only 12 km road segment have been completed so far. Community Development Support: 5 Irrigator's Associations were formed and workshops were conducted to assess the current status of cooperatives. 31 out of the targetted 50 municipal extension staff were trained on IPM amd 139 farmers graduated from the Farmers Field School on IPM. The LBP has agreed to provide agricultural credit to farmers' cooperatives in the project area. Social Services: 16 Day Care Centers out of the global target of 35 DCCs have been completed and 35 day care workers have been trained. 17 units frp, a target of 27 Brgy. Health Stations have also been completed. 1 Municipal Health Ctr from a target of 3 units was completed. The sites for the 4 water supply systems have been identified and construction were undertaken in 3 sites.
11 Metro Cebu Development Project I (MCDP I)	Japan/ OECF	Provincial Government of Cebu, DPWH (for the national roads component)	The project involves construction/improvement of 14 links of arterial roads, bridges and cause way in Cebu through the DPWH; and upgrading of public market and provision of technical assistance.	1989-1995	(Forex: Y2.063 b)	2.70% (Interest rate) 20 years (Maturity period) 10 years (Grace period)	Province of Cebu	14% per annum 15 years repayment period, inclusive of a three-year grace period.	For national roads, LGU to provide ROW acquisition as counterpart.	The roads components are provided as grant from national government to the province.
12 Community-Based Resource Management Program (CBRMP)	WB	DOF (Executing Agency) DENR, DA-BFAR, DILG and LGUs (Implementing Agencies)	The project aims to reduce rural poverty and environmental degradation through support for locally generated and implemented natural resource management projects. The specific development objectives include: (a) to improve management of upland and forestry resources indicated by a reduction in deforestation, increased vegetation cover and reduced soil erosion; (b) to improve coastal and near shore fisheries resources indicated by an expansion in mangroves and a reversal of the decline in catches of fisheries; and (c) to improve infrastructure in support of management of upland, coastal and near shore natural resources as indicated by improvements in rural roads, water supply and sanitation facilities, irrigation systems and other small-scale infrastructure. The project components include: a. LGU Institutional Development - enhancement of LGUs and communities capacity to plan, implement and sustain priority natural resource management projects through training by DILG's Local Government Academy and community organizers including provision of training materials, equipment and training fees. b. Project Management and Environmental Technology Transfer and Policy - enhancement of financial	1998-2004	3,600.97 (Forex $50.0 m) (Local: NG-DOF: P155.32 m; P1,017.31 m inclusive of equity, travel costs, labor and contingency)	LIBOR base rate plus LIBOR total spread (Interest Rate) 0.75% (Commitment Fee) 20 years (Maturity period) 5 years (Grace period)	**Provinces Identified:** Albay Camarines Norte Camarines Sur Catanduanes Sorsogon Masbate Bohol Cebu Negors Oriental Siquijor Biliran Eastern Samar Leyte Northern Samar Western Samar Southern Leyte Agusan del Norte Agusan del Sur Surigao del Norte Surigao del Sur	14% per annum 15 years repayment period, inclusive of a three-year grace period.		DENR assists in the policy and technical assistance component. The project is a combination of a loan and grant to the beneficiaries. A total of 56 LGUs have availed of the facility.

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			management capacity of central government systems and their capacity to transfer environmental technology, and the improvement of environmental policies implementation. c. Sub-projects in Natural Resources Management - carrying out of specific LGU community-based resource management investment projects through the provision of loans and grants for the following: (1) upland agriculture; (2) community forestry; (3) coastal resources and near shore fisheries; (4) rural infrastructure; and (5) small-scale livelihood investments.							
13 Metro Cebu Development Project Phase II (MCDP II)	Japan/ OECF	Provincial Government of Cebu RDC VII	The project involves the construction of infrastructure in Metro Cebu, such as the bus terminal, sanitary landfill and public market.	1990-1997	(Forex Y4.30 b)	2.70% (Interest rate) 20 (Maturity period) 10 (Grace period)	Two cities have availed of the facility: Talisay City -market Mandaue City - market	14% per annum. 15 years repayment period, inclusive of a three-year grace period.	LGU to provide ROW acquisition as counterpart.	
14 Subic Bay Area Municipal Development Project (SBAMDP)	ADB (loan) Spain (grant)	DILG (Lead) SBMA and LGUs	The project aims to improve the living conditions and public health standards in particular, and the urban environment in general by providing infrastructure such as roads and bridges, flood control and drainage, public markets and solid waste management. It also aims to assist LGUs to enable them to develop their institutional capacity.	1998-2003	(Forex/Loan Amount for LGUs: $17.62 m; and $4.38 m for LWUA)	Variable (Interest rate) 0.75% (Commitment fee) 25 years (Maturity period) 3 years (Grace period)	Olongapo City, Zambales Subic Town, Zambales Castillejos, Zambales Dinalupihan, Bataan Hermosa, Bataan Morong, Bataan San Marcelino, Zambales	14% per annum 15 years repayment period, inclusive of a three-year grace period.	LGUs to provide counterpart funds from their own resources in cash and payments in kind to cover certain local currency including costs on land acquisition, incremental administraion and local civil works. Percentage cost-sharing in maximum sub-loan and counter-part fund for LGUs: Castillejos - 78% subloan; 22 % LGU counterpart fund Dinalupihan - 63% SL; 37% LGU Hermosa - 78% SL, 22% LGU Morong -78% SL; 22% LGU San Marcelino - 78% SL; 22% LGU Subic Town - 78% SL, 22 % LGU Olongapo City- 78% SL, 22% LGU	A cancellation of $13.4 million from the loan proceeds due to cancellation of several sub-projects in Castillejos San Marcelino and Hermosa; and expand the existing water supply facilities in Morong. LWUA-PMO completed preparatory works in all concerned LGUs required for the FS while detailed engineering design for completion. Other infrastructure subprojects are in various states of implementation, as follows: 1. Subic - equipment for solid waste will be delivered on 30 Nov 2001. 2. San Marcelino - D/E for the public market will be completed on 29 Nov. 2001; pre-qualification of contracts is ongoing. 3. Dinalupihan - advertisement for the procurement of solid waste equipment was made on 3 Oct 2001 while D/E for the access road is ongoing. 4. Hermosa - issuance of bid documents for the procurement of equipment was made in mid Nov while D/E for the access road is ongoing. 5. Morong - bidding for the procurement of equipment is ongoing. 6. Olongapo - preparation of F/S for Elicano Bridge is ongoing.
15 Clark Area Municipal Development Project (CAMDP)	ADB	DILG (Executing) DPWH, BCDA and LGUs (Implementing agencies)	The project aims to construct, upgrade and rehabilitate basic urban infrastructure facilities covering solid waste management, urban roads, drainage and flood control through implementation of separate sub-projects. It also aims to assist LGUs to develop institutional capability by implementing programs for human resources development and productivity enhancement.	1999-2005	(Forex/Loan Amt: $24.23 m)	Variable (Interest rate) 0.75% (Commitment fee) 20 years (Maturity period) 5 years (Grace period)	Angeles City Tarlac City Municipality of Bamban Municipality of Capas Municipality of Concepcion Municipality of Mabalacat Municipality of Magalang Municipality of San Fernando	14% per annum. 15 years repayment period, inclusive of a three-year grace period.	LGUs to provide counterpart funds from their own resources in cash and payments in kind to cover certain local currency including costs on land acquisition, incremental administraion and local civil works. Percentage cost-sharing in maximum sub-loan and counter-part fund for LGUs: Angeles - 60% SL; 40% LGU Tarlac - 67% SL; 33% LGU Bamban - 68% SL; 32% LGU Capas - 87% SL; 13% LGU Concepcion - 96% SL, 4% LGU Mabalacat - 96% SL, 4% LGU Magalang - 88% SL, 12% LGU San Fernando - 79% SL, 21% LGU.	Delays in implementation of physical components by almost 2 years have been experienced. These are due to delays in loan effectiveness and other start-up activities, like delayed establishment of DILG's full PMO, delayed signing of the sub-loan agreements for physical infrastructure components between MDFO and LGUs, LGUs lack of enthusiasm for implementing their sub-project, and delayed re-computation of the borrowing capacities/limits of the LGUs. On solid waste management (installation of 2 inter-municipal landfill sites and provision of equipment in all 8 LGUs), Angeles City and Conception proposed to include the Ecological Solid Waste Management System under the project.

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										On the flood control and drainage component for canals in Bamban, Capas and Tarlac, detailed engineering for Tarlac has been completed. On urban roads and drainage (roads improvement of about 7 km widening of 2 bridges, rehabilitation of 1 bridge and construction of an additional bridge), Hensonville Bridge in Angeles City was already completed by DPWH.
16 Southern Philippines Irrigation Sector Project (SPISP)	ADB	NIA (Executing Agency) Provincial Government of Agusan del Norte (Executing Agency) DOH, DENR	The project involves the construction and improvement of small- to medium-scale irrigation systems, strengthen operation and maintenance through beneficiary participation, and institutional capacity of executing agencies. In the Southern Philippines, the project will develop irrigation and drainage facilities covering about 18,000 hectares for intensive cultivation of rice and other crops. The specific components are: a. Beneficiary participation and management of irrigation systems - includes training; b. Physical infrastructure - development of national irrigation systems, communal irrigation systems, small reservoir irrigation systems and construction of about 60 km of access and service roads. c. Environmental and social measures - community-based forestry and schistosomiasis control.	1999-2006	TPC: $102 m (Forex/Loan Amount -$60 m) (GOP $33.1 m) (Beneficiaries $8.9 m)	Interest rate is determined in accordance with ADB's pool-based variable lending rate 25 years (Maturity period) 7 years (Grace period) 0.75% p.a. (Commitment fee)	Buenavista, Agusan del Sur	14% per annum 15 years repayment period, inclusive of a three-year grace period.	Beneficiaries will provide 25% of total construction cost of sub-projects, broken down as 15% labor, 10% equity contribution including cash, ROW, land for the implementing agency's office, and post-harvest facilities.	Release has been made to the Province for the Calagayan-Agong Ong Communal Irrigation System
17 Southern Mindanao Integrated Coastal Zone Management Project (MALALAG)	JBIC	Department of Environment and Natural Resources (DENR), LGUs, (Cotabato), DOF	The project aims to undertake the implementation of an integrated environmental protection and management of critical ecosystems as imperative to sustainable development. It also aims to (a) integrate the management of a coastal and watershed ecosystem in the project sites; (b) undertake activities that will sustain resource and environmental management while allowing development; (c) improve the quality of life of beneficiaries and stakeholders given available resources; (d) insitutionalize the use of integrated management approach vis-à-vis carrying capacity of the area; and, (e) develop capability of LGUs and stakeholders in the planning and sustainable management of natural resources and environment.	1999-2007	1,219.00 (Forex: $914.57 m) (Local: P304.43 m)	1.7% p.a. for civil works and 0.75% p.a. for other components (Interest Rates) 20 years for civil works and 30 years for other components (Maturity Period) 3 years (Grace Period)	Provinces Identified: General Santos City South Cotabato Sarangani Davao del Sur Project Sites and Scope of Work 1. Sarangani Bay - Mt. Matutum Watershed (Gen. Santos City, Sarangani and South Cotabato) a. Afforestation b. Environmental Center c. Sewage Treatment d. Civil Works e. Livelihood Support 2. Malalag Bay - Balasiao Watershed (Davao del Sur) a. Afforestation b. Equipment c.Livelihood Support d. Civil Works (to be implemented by the Municipal Government of Malalag)	14% per annum. 15 years repayment period, inclusive of a three-year grace period.	For the construction of farm-to-market roads: LGUs to cover 15% of the P6.3 million for this component (processing thru MDF). For the water supply component, LGUs will put up 15% of the P7.8 million (thru the MDF processing).	For the sub-loan component, no releases have been made by MDFO.
18 LGU Finance and Development Project (LOGOFIND)	WB	DOF (Lead), DILG LGUs	The project provides financing for LGU urban projects for expansion, upgrading basic infrastructure, services and facilities through the establishment of urban loan window/facility within the Municipal Development Fund. It also provides TA and institutional support to strengthen LGUs' capacity in municipal governance, investment planning, revenue generation and enhance their capacity to support and finance local government development and investment.	1999-2006	4,000.00 (Forex/Loan Amount $100 m)	LIBOR base rate + LIBOR total spread (Interest rate) 0.75% (Commitment fee) 20 years (Maturity period) 5 years (Grace period)	Nationwide	14% per annum. 15 years repayment period, inclusive of a three-year grace period.	LGUs are required to provide 10% of the total subproject cost, in materials, cash or services in the planning and supervision of the sub-project.	Cancellation of $40 million has been approved. Under the subproject component, 260 LGUs have expressed interest to participate in the project, of which 35 LGUs have completed feasibility studies, 28 LGU subprojects appraised, 13 LGU subprojects approved by the Policy Governing Board (PGB). Five of these LGU subprojects have approvd detailed engineering plans and 5 LGUs are currently on the process of detailed engineering preparation. Four LGUs have completed civil works bid documents, 2 of which are in the process of evaluating civil works bids. Several training/orientation sessions for LGUs have been conducted. These include training on F/S

Program/Project Title	Funding Institution	Implementing Agency	Description	Duration	Loan Amount (In Million Pesos)	Terms and Conditions of Funding Institution	Location	Re-Lending Terms and Conditions	Cost-Sharing Arrangements	Status/Remarks
										preparaton attended by 10 LGUs, Orientation Conference for Visayas and Mindanao regions. On LGU Resource Mobilization, the LGU Performance Monitoring Study has been completed. The TOR for the redesigning of the Real Property Tax Administration has been revised based on WB comments and submitted to the Bank for final approval. Disbursement for Dalaguete, Cebu made for its public market project.
19 Metro Iligan Regional Infrastructure Development Project (MIRIDP)	JBIC	Provincial Government of Lanao del Norte (Implementing Agency)	The project involves the construction of off-site infrastructure facilities supportive of the development of the Metro Iligan Regional Infrastructure Development Project located in Linamon, Lanao del Norte.	1999-2008	(Forex/Loan Amount: Yen 4.33 b)	2.20% (Interest rate) 20 years (Maturity period) 10 years (Grace period)	Lanao del Norte province	14% per annum. 15 years repayment period, inclusive of a three-year grace period.	For roads: 80% National govenent and 20% LGU. For hydroelectric power plant: 10% national government and 90% LGU.	No releases have been made by MDFO to the Provincial Government for the project.
20 Mindanao Rural Development Project (MRDP)	WB	Department of Agriculture (DA), BFAR DENR, LGUs, MDFO	The project involves capacity building of LGUs, particularly provincial governments in Mindanao, to develop and carry out sound agricultural development policies and programs of the DA. Its components include: (a) Rural infrastructure (rehabilitation and a. Rural infrastructure (rehabilitation and maintenance of provincial and farm-to-market roads, rehabilitation and construction of selected communal irrigation systems, establishment and upgrading of spring development schemes; b. Community development sub-projects which meet community preferences and respond to national government priorities for supporting small-scale agricultural and fishery development; c. Institutional and implementation support for micro-finance institutions and cooperatives, LGUs, project coordination office; and, d. Coastal and marine biodiversity conservation.	2000-2003	1,370.76 (Forex: $27.5 m in loan and P50 m in grant funds) (Local: P220.76 m)	LIBOR base rate + LIBOR total spread (Interest Rate) 3/4 of 1% p.a. on the principal amount (Commitment Fee) 20 years (Maturity Period) 5 years (Grace Period)	Provinces Included under APL-1: North Cotabato Sultan Kudarat Maguindanao Compostela Valley Agusan del Sur	14% per annum. 15 years repayment period, inclusive of a three-year grace period.	Cost-sharing in terms of TPC: DA - 14% LGU - 14% Others - 74% broken down as follows: Beneficiaries - 1% GEF Grant - 3% Loan Proceeds - 68%	Rural Infra Component: several farm-to-market road and bridge projects have been awarded, including water supply projects and conduct of detailed engineering for communal irrigation projects. Community Fund for Agricultural Development: For all 11 municipa-lities in Cotabato and Sultan Ku-darat, social preparation activities are in various stages of implemen-tation. Coastal and Marine Biodiversity Conservation: Consultations with all LGUs and stakeholders have been conducted. Coordination activities completed with fisheries schools, national line agencies and NGOs/POs.
B. Line Agencies										
21 Municipal Solar Infrastructure Project (MSIP)	AusAID EFIC	DILG	The project involves the (a) provision of photovoltaic systems in 403 barangays identified as part of the SRA (9 provinces in Visayas and Mindanao); and, (b) training of community groups in the administration, operation and maintenance of these systems. This would improve the quality of life of the intended beneficiaries by upgrading the delivery of health and other basic services, education and water supply facilities.	1997-2001	1,367.99 (Forex $28.02m) (Local P255.98 m)	3.40% (Interest rate) 10 years (Maturity period) 7.5 years (Grace period)	Guimaras Antique Biliran Eastern Samar Bohol Leyte Surigao del Sur Sulu Tawi-tawi	No data available.	LGU counterpart activities include development of buildings, development of water source, improvement of buildings for Barangay Halls and Barangay health centers.	completed.
22 Rural Infrastructure Development Project (RIDP)	ADB	DA	The project aims to increase production, productivity and diversity of rice and corn-based smallholder farming systems thereby raising disposable income. It also aims to improve standard of living of rural popu-lation by facilitating access to social services. The specific components are: a. Infrastructure - rural roads, communal irrigation systems, storage facilities; b. Agricultural Support Services - extension services, agricultural research, communication and info delivery, cooperative development component for farmers organizations; and, c. Project management.	1995-2001	TPC: $26.62 m (ADB Loan: $17.5 m) (GOP: $9.12 m)	Variable (Interest rate) 1% (Service charge) 25 years (Maturity period) 5 years (Grace period)	Zamboanga del Norte - Municipalities of Kalawit, Tampilisan, Gutalac, and Labason. Zamboanga del Sur - Municipalities of Titay, Ipil and Payao.	No data available.	**Civil works:** Roads and bridges - DA- 50%; LGU - 30%; ADB Loan Proceed 20%. Warehouses - DA-68%, LGU - 12%; ADB LP - 20% Irrigation - DA-80%; ADB LP-20%. **Equipment and vehicles:** With imported parts - ADB LP 100%; With no imported parts-DA - 100%. **Operations and Admin -** DA- 80%; ADB LP - 20% **Training** - DA 100%	completed.

Sources: Various reports and documents from DOF-MDFO, NEDA, executing/implementing agencies, and donor country programs.

ANNEX II-B
Grants to Local Government Units for Capital Outlays
As of end December 2001

Program/Project Title	Funding Institution	Implementing Agency	Description	Duration	Loan/Grant Amount (In Million Pesos)	Terms and Conditions of Funding Institution	Location	Cost-Sharing Arrangements	Status/Remarks
A. *Health*									
1 Early Childhood Development Project (ECDP)	WB ADB	DSWD (lead) DECS DOH LGUs	The ECD Project is a six-year operationalization of the 10-year national ECD Program in three targeted regions (6, 7,12). It aims to reduce by half the infant mortality rate, child mortality rate, protein-energy malnutrition, and drop-out rates in elementary schools; improve psychosocial development and school-preparedness of children and the achievement level of grade 1 pupils; and support local government initiatives and fund resources for ECD, partnership of national, regional and local government and activities of family and communities as child care givers. The following interventions are expected to meet these objectives: a. ECD Service Delivery - Program support for provincial LGUs through expanded program of immunization (to be managed by the DOH MCH Service); Integrated management of child illness (DOH-MCHS); Micronutrient malnutrition prevention and control (DOH Nutrition Service); Parent effectiveness service (DSWD in coordination with DECS); and Grade 1 ECE/ECD (DECS); and, Financing facility for municipal/city LGUs of ECD Sub-projects (to provide matching financing, on a flexible cost-sharing bases geared to LGU income levels but full funding by LGUs of recurrent costs for LGUs wishing to upgrade ECD services; b. Support to service delivery - Support to communications, planning, targeting and MIS, training and institutional development; and, c. Research and Development.	1998-2004 (WB) 1998-2005 (ADB)	2,352.00 (Forex $43.5 m) (ADB $24.5m) (WB $19 m) (Local/GOP P724 m)	ADB OCR: 6.8% interest rate, 1% service charge, 25 years maturity period, 5 years grace period. ADB ADF: 0.08% interest ratem 1% service charge, 25 years maturity period, 5 years grace. WB: LIBOR + 1/2 of 1% interest rate, 3/4 of 1% service charge, 16 years maturity period, 5 years grace period.	**Provinces Identified:** Guimaras Capiz Iloilo Antique Negros Occidental Negros Oriental Cebu Bohol Lanao del Norte North Cotabato Aklan Siquijor Sultan Kudarat	Provided as grant from NG to LGU, except on financing for ECD subprojects where LGUs will pay for recurrent costs and a flexible cost-sharing arrangement based on the LGU income level will be followed.	The joint WB-ADB mid-term review resulted to the following recommendations, among others: 1. Reduction in ADB loan funds of at least $2.4 M (coming from savings such as reduction in the amount required for EPI cold chain procured under WB and operating cost allocation which should not be paid by the loan) 2. Possible reallocation of loan proceeds across categories to accommodate increase in ADB share of LGUFF expenditure items (taking note not to change the final 60-40 cost-sharing of the OCR loan).
2 Korea-Philippines Friendship Medical Hospital	Korean Government through the Korean International Cooperation Agency (KOICA)	Provincial Government of Cavite	The project aims to build a 100-bed annex hospital of the Andres Memorial Hospital fully equipped with modern facilities and equipment. The hospital building will have an approximately 4,000-square meter floor area. A branch clinic will also be established near Cavite Export Processing Zone in Rosario, Cavite. The specific components are: a. Civil works; b. Equipment provision; c. Dispatch of Korean experts; and, d. Training.	2000-2004	(Forex $3.8 m)	Grant	Cavite	LGU to provide land and pay for taxes and duties.	The project faces delays because the Provincial Government has yet to submit to KOICA the required land titles under the province of Cavite, The provincial government is currently fast tracking the release of the documents in close coordination with all concerned agencies.
B. *Education*									
3 Third Elementary Education Project (TEEP)	WB Japan/JBIC	DECS	The project aims to raise the participation of school age children, improve the six-year completion in elementary schools, and increase academinc achievement. Key functions will be moved from the central and regional levels to the divisions and schools. The project will finance two major components: a. Component I - enhancing the capability of central and regional DECS through the provision of technical assistance, training, equipment, supplies and materials, and operation costs; and, b. Component II - enhancing the capability of Division/ District offices and schools in the areas of educational planning and management, instructional supervision, administrative, information and financial management, improving LGU and community participation, instructional effectiveness. The project will finance technical assistance, training, equipment, physical facilities and incremental MOOE.	1997-2004 (WB) 1997-2006 (JBIC)	16,915.24 (Forex $218.18 m) (Local- from Nat'l Gov't P8,923.91 m; from LGUs - P1,507.9 m)	LIBOR rate plus LIBOR total spread (WB interest rate) 2.70% (JBIC interest rate) 0.75% on principal not withdrawn (WB commitment fee) 20 years (WB and JBIC maturity period) 5 years (WB grace period) 10 years (JBIC grace period)	Provinces Identified per Phase: Phase I: WB - Ifugao, Antique, Agusan del Sur; JBIC-Benguet, Surigao del Sur, Guimaras. Phase II: WB-Southern Leyte, Zamboanga del Sur, North Cotabato; JBIC-Romblon, Masbate, Negros Oriental, Biliran, Leyte Phase III: WB-Batanes; JBIC-Mountain Province, Abra, Kalinga, Apayao, Aurora, Capiz, Eastern Samar.	LGUs to provide 25% as counterpart for the school buildings component. The remaining 75% is provided as grant by NG to LGUs.	The restructuring was approved which includes the implementation of the DECS-led school building program and the introduction of Elementary Leader Schools approach. School Building component - as of date accomplishment includes 507 new classrooms constructed and 796 repairs. Construction of 1,864 new classrooms and 1,769 repairs are currently ongoing. The significant increase in completion was brought about by the parallel implementation of the DECS-led and LGU-led.
4 Secondary Education Development and Improvement Project	Japan/JBIC and ADB	DECS (Executing Agency) Bureau of Secondary	The project is a follow-up to the six-year Secondary Education Development Project (SEDP) which was completed in 1994. The project aims address the	2000-2006	6,764.00 (ADB Forex/Loan Amount $53 m)	ADB terms: Variable (Interest rate)	26 Provinces Ifugao, Benguet, Antique, Guimaras, Agusan del Sur,	No data available.	Among themore significant accomplishments include: 1) the completion of the Training

Program/Project Title	Funding Institution	Implementing Agency	Description	Duration	Loan/Grant Amount (In Million Pesos)	Terms and Conditions of Funding Institution	Location	Cost-Sharing Arrangements	Status/Remarks
(SEDIP)		Education (Implementing agency)	gaps which SEDP was not able to do during its implementation phase. It is also a complementary sequal project to the Third Elementary Education Project (TEEP). The project will cover the priority areas identified under the Social Reform Agenda		(JBIC Forex/Loan Amount $59.96 m)	0.75% (Commitment fee) 20 years (Maturity period) 5 years	Surigao del Sur, Romblon, Masbate, Negros Oriental, Leyte, Southern Leyte, Biliran, Zamboanga del Sur, North Cotabato, Abra, Mt.		Program on Project Proposal Preparation; 2) signing of the Memoranda on School Bldg. for the 6 batch 1 provinces; 3) procrement of office equipment
			(SRA) and by the PCFP.			(Grace period)	Province, Kalinga, Apayao, Sulu, Tawi-tawi, Maguindanao Batanes, Aurora, Capiz, Eastern Samar, Basilan		for the NPMO; 4) approval of the resolution to award for the procurement of textbooks and teachers' manuals; and 5) DBM's confirmation of the CY 2002 budget level for the project.
C. *Agriculture and Agrarian Reform*									
5 Agrarian Reform Communities Development Project (ARCDP)	WB	DAR (Lead/Executing Agency) NIA (implementing agency) and LGUs (implementing agency)	The project involves the provision of basic rural infrastructures, agricultural and enterprise development activities and strengthening of cooperatives in 100 Agrarian Reform Communities (ARCs) located in 10 provinces over a period of six years. The components are: a. Communal Irrigation Systems/Projects; b. Rural Access - Roads and Bridges; c. Community Infrastructure - Potable Water Supply, Multipurpose Centers; d. Community Development and Technical Assistance; and, e. Agricultural and Enterprise Development.	1997-2003	3,271.00 (Forex $31.9 m) (Local P2,283 m)	1/2% of 1% LIBOR (Interest rate) 3/4% of 1% (Commitment fee) 20 years (Maturity period) 5 years (Grace period)	A total of 102 ARCs have been assisted by the project since 1997 in the following provinces: Ilocos Norte Isabela Quezon II Albay Leyte Southern Leyte Davao Oriental Davao del Norte Misamis Oriental Surigao del Norte	By project component: I. Roads and Bridges a. 1st - 3rd class municipalities: 80% from WB/loan proceeds and 20% from LGU/ARC; b. 4th - 6th class: 90% from WB/LP and 10% from LGU/ARC. II. Water supply system a. 1st - 3rd class: 70% from WB/LP, 20% from LGU and 10% from ARC b. 4th - 6th class: 80% from WB/LP, 10% from LGU and 10% from ARC III. Multi-purpose center a. 1st - 6th class: 50% from WB/LP, 30% from LGU and 20% from ARC. IV. Irrigation a. 1st - 3rd class: 90% from WB/LP and 10% from GOP. No LGU/ARC share required. 50 years payable to NIA. b. 4th - 6th: 70% WB/LP and 30% LGU/ARC but no amortization required.	The project has been performing relatively well, achieving more than 75% of their targets under each component, including the utilization rate.
6 Belgian Integrated Agrarian Reform Support Programme (BIARSP)	Belgian Administration for Development Cooperation	DAR	The project is an expansion of the BIARSP Project covering orginal target areas as well as new expansion areas in Siquijor, Zamboanga and Basilan. The project also provides support activities for public health and social security, elementary education and potable water supplies and sanitation. Project components include: (a) Agricultural productivity and rural infrastructure, irrigation, (b) Basic education services, (c) primary health care services, (d) drinking water supply/sanitation services.	1998-2002	992.00 (Forex: BEF 900 m) (Local P272 m)	Grant	Provinces Identified: Bohol Cebu Negros Oriental Siquijor Zamboanga del Norte Zamboanga del Sur Basilan	Provided as grant from NG to LGUs. LGUs, however, have to contribute in cash or in kind for infrastructure projects.	The project, as reported by DAR, has posted a very high accomplishment rate since it has exceeded almost all of its targets under each specific component.
7 Agrarian Reform Communities Project (ARCP)	ADB	DAR (lead), with assistance from the following agencies: NIA, Land Management Bureau, MDFO, LBP, ARMM and LGUs.	The project involves rehabilitation and construction of farm-to-market roads and bridges, culverts; rehabilitation of existing 140 ARCs, improvement/rehabilitation of existing wells, installation of additional wells and development of spring sources, survey of 100,000 ha. of public alienable and dispensable lands and distribute land titles to beneficiaries; introduce alternative farming systems and small enterprise to cooperatives and agrarian reform beneficiaries; provide trainings and credit facilities to extension workers, leaders and cooperatives on enterprise planning and management. The components are: a. Rural infrastructure - access infrastructure such as roads and bridges, water supply and irrigation; b. Land survey;	1999-2005	7,237 (Forex $51.4 m) (Local P5,035 m)	6.76% (Interest rate) 0.75% (Commitment fee) 25 years (Maturity period) 6 years (Grace period)	35 Provinces Identified: Abra, Benguet, Ilocos Sur, La Union, Pangasinan, Cagayan, Quirino, Nueva Viscaya, Nueva Ecija, Palawan, Catanduanes, Masbate, Sorsogon, Antique, Guimaras, Capiz, Iloilo, Aklan, Western Samar, Northern Samar, Biliran, Bukidnon, Camiguin, Misamis Occ., Davao del Sur, South Cotabato, Saranggani, Davao Province, Sultan Kudarat, Lanao del Norte, North	For the Rural Infrastructure Component: a. Rural Roads 1st - 3rd class municipalities 80% - ADB/LP; 20% - LGU/ARC Equity 4th - 6th class municipalities 90% - ADB/LP; 10% - LGU/ARC Equity b. Water supply - regardless of class - 70% ADB/LP (grant to LGU); 30% LGU/Irrigators Association (10% could be in kind from the community)	

Program/Project Title	Funding Institution	Implementing Agency	Description	Duration	Loan/Grant Amount (In Million Pesos)	Terms and Conditions of Funding Institution	Location	Cost-Sharing Arrangements	Status/Remarks
			c. Development support - agricultural development support (agricultural technology dissemination and delivery system and credit needs of ARBs, POs and cooperatives); rural enterprise development support (business advisory services, training, marketing, etc.); community and institutional development (organiza-				Cotabato, Surigao del Sur, Lanao del Sur, Sulu, Maguindanao, Tawi-tawi	c. Potable Water Supply - of class - 70% ADB/LP (grant to LGU); 30% LGU/ARC (10% could be in kind from the community).	
			tional capacity building, gender and development, etc); d. Credit facilities - through the Land Bank of the Philippines.						
8 Poverty Alleviation for SRA: Support to Selected ICCs and ARCs in Mindanao (PAPSRA)	CIDA under the Phil-Canada Development Fund	DAR	The project involves the conduct of research studies on specific development interventions that addresses the needs of indigenous people, fisherfolk and the urban people, formulation of local framework of poverty alleviation; improvement of resource allocation and utilization process for SRA; construction of basic infrastructure such as farm-to-market roads, health centers, bridges, solar dryers and potable water systems; and provision of agri-industrial livelihood support projects.	1999-2002	87.10 (Forex $1.92 m) (Local P12.10 m)	Grant	Zamboanga del Norte Zamboanga del Sur South Cotabato Sultan Kudarat Davao del Sur Cotabato	Provided as grant from NG to LGUs. LGUs, however, have to contribute in cash or in kind for infrastructure projects, such as land acquisition or right-of-way.	The project was not able to meet its overall target of completing 115 projects. There are still more than 20 ongong or nearing completion and several projects have recently started.
9 Second Kennedy Round 2 (KR2)	Japanese Government	NEDA (lead), DA, NAFC	The program is a commodity assistance whose proceeds are used to support activities in the following sectors: a. Agriculture - small post harvest facilities, animal health services, ARC support, small scale irrigation, LGU-sponsored NGO livelihood projects, farm inputs support, fertilizer procurement; b. Health - construction of toilet and basic training on sanitation, and immunization program; c. Education - technical vocational training/skills training and provision of equipment; and, d. Environment - mangrove rehabilitation, bay management, and sanctuaries. The proceeds are also used for the Project Development Fund for LGUs to undertake the following: a. Master planning; b. Pre-investment studies; c. Pre-feasibility studies; d. Feasibility studies; and e. Project monitoring.	Since 1976 use of proceeds for LGU projects started in 1995 and continuing	Yen 1.65 b (annual estimate)	Grant	Regions V and IX (pilot) Regions VIII, XII and CAR (expansion areas)	Provided as grant from NG to LGUs. Local counterpart from LGUs is 20% of total project cost provided in cash or non-cash/in-kind.	
10 Agrarian Reform Infrastructure Support Project, Phase II (ARISP II)	JBIC	DAR, NIA, DPWH, Municipal LGUs	The project aims to reduce poverty incidence through the increase of agricultural productivity and income of farmers in Agrarian Reform Communities nationwide by providing basic infrastructure, establishing/strengthening farmers' organizations and strengthening local government units. The project components are: a. Construction of basic infrastructure - irrigation and drainage facilities, farm-to-market roads, post-harvest facilities and rural water supply systems; b. Insitutional development - farmers' cooperatives and irrigators association; c. Procurement of equipment.	2000-2007	6,740.00 (Forex $147.25 m) (Local P1,077 m)	1.8% (Interest rate) 20 years (Maturity period) 10 years (Grace period)	Nationwide coverage in 55 provinces.	By project component: I. Roads and Bridges a. 1st - 3rd class municipalities: 80% from JBIC/loan proceeds and 20% from LGU/ARC; b. 4th - 6th class: 90% from JBIC/LP and 10% from LGU/ARC. II. Water supply system a. 1st - 3rd class: 70% from JBIC/LP, 20% from LGU and 10% from ARC b. 4th - 6th class: 80% from JBIC/LP, 10% from LGU and 10% from ARC III. Irrigation a. 1st - 3rd class: 90% from JBIC/LP and 10% from GOP. No LGU/ARC share required. 50 years payable to NIA. b. 4th - 6th: 70% JBIC/LP and 30% LGU/ARC but no amortization required.	The project has recently started and certain compoennets such as the construction of post-harvest facilities and the establishment of rural water supply facilities have yet to commence.

Program/Project Title	Funding Institution	Implementing Agency	Description	Duration	Loan/Grant Amount (In Million Pesos)	Terms and Conditions of Funding Institution	Location	Cost-Sharing Arrangements	Status/Remarks
11 Support to Agrarian Reform Communities in Central Mindanao (STAR-CM)	EU	DAR	The project aims to increase the self-reliance, living standards and quality of life for all households that are actively farming in 50 selected agrarian reform communities in four provinces in Central Mindanao. The project components are: (a) institutional a. Institutional strengthening - a broad-based capacity building and organizational development and a more technically oriented training covering specific topics to assist ARCs and LGUs in their	2000-2009	Euro 23.33 million (Forex Euro 18.42m) (Local 4.903 Euro m)	Grant	Sultan Kudarat North Cotabato Lanao del Norte Lanao del Sur	Provided as grant from NG to LGUs. LGU contribution in cash or in kind for infrastructure projects, such as land acquisition, ROW, local labor, etc.	The project has just started.
			functions; b. Support infrastructure - construction/rehabilitation of 170 km of feeder roads, construction of 150 ha. of new and communal irrigation systems; and 800 has. of rehabilitated communal irrigation systems; and provision of at least 1 potable water systems and multi-purpose building per ARC; c. Agricultural productivity and access to rural finance - improved crop inputs, land preparation, harvest and processing machinery; and draft and production livestock.						
D. ***Water Resources***									
12 First Rural Water Supply and Sanitation Sector Project	WB	DPWH (for water supply component and pilot monitoring and evaluation) DILG and DOH (cooperating agencies)	The project aims to improve the living conditions of the rural population through the provision of additional water supply and sanitation facilities in areas deemed to have the most urgent need for such facilities. The specific components are: a. Construction of level I systems including shallow wells, deep wells, spring developments, rain water collectors, workshop buildings and pilot water treatment units; b. Rehabilitation of wells; c. Formation of Barangay Waterworks and Sanitation Associations; d. Provision of sanitary facilities such as family latrines, well disinfectations, sanitary well protection facilities, public toilets, sullage removal units, and pilot wastewater treatment units.	1991-1996 (?)	No data available.	No data available.	Water supply component in rural areas in Luzon - 28 provinces: La Union, Cavite, Tarlac, Nueva Ecija, Albay, Sorsogon, Camarines Sur, Camarines Norte, Bulacan, Bataan, Pampanga, Batangas, Laguna, Ifugao, Mt. Province, Masbate, Marinduque, Palawan, Quezon, Catanduanes, Romblon, Cagayan, Kalinga-Apayao, Quirino, Aurora, Isabela, Pangasinan, Benguet	NG - 80% of TPC LGU - 10% of TPC BWSA - 10% of TPC NG component provided as grant to LGUs. LGU contribution may be in cash or in kind for labor, land acquisition, etc.	Completed.
13 Rural Water Supply and Sanitation Sector Project (RW3SP)	ADB	DPWH (Executing Agency) DILG and DOH (cooperating agencies) LGUs (implementing agencies)	The project aims to improve the capacity of sector agencies in enhancing the delivery of social services, provide safe, adequate and reliable WSS services to selected low-income rural communities and support health and hygiene education, water quality surveillance and community management activities. The specific components are: Part A - Institutional Development a. Capacity building program for LGUs in organizational management, technical and financial aspects of project implementation; b. Community management training focused on WS operations and maintenance, organizational management and financial development; c. Health and hygiene education program; and, d. Water quality control and surveillance program. Part B - Water Supply and Sanitation Facilities a. Construction and rehabilitation of point source (Level 1) water supply systems and provision/ construction of sanitation facilities.	1998-2002	TPC $57.4 m (Forex/Loan Amount $37 m) (GOP $20.4 m)	Variable (Interest rate) 0.75% (Commitment fee) 20 years (Maturity period) 5 years (Grace period)	Provinces Identified: Abra, Apayao, Benguet, Kalinga, Ifugao, Mt. Province, Batanes, Aurora, Romblon, Masbate, Antique, Guimaras, Biliran, Eastern Samar, Southern Leyte, Basilan, Agusan del Sur, Surigao del Sur, Sulu and Tawi-tawi	80% from loan proceeds (ADB), 10% from the province and the remaining 10% is from the recipient barangays through labor and indigenous materials, and operations and maintenance for district laboratories and public toilet.	The overall implementation is about 2 years behind schedule to delay in loan effectiveness and late recruitment of consultants. Low physical accomplishment was also noted due to lack of well drilling equipment and the lack of technical capability of the LGUs.
14 Rural Water Supply and Sanitation Project, Phase V	Japanese Government through JBIC	DILG (Executing Agency) Provincial and Municipal Governments (Implementing agencies)	The project aims to strengthen LGU capability in planning, implementing and managing of water and sanitation projects through the provision of water supply (Level 1) and sanitation facilities to 5th and 6th class municipalities of the identified six provinces. It also aims to promote sustainability through community participation, operation and maintenance of water supply system and promote proper health and hygiene and monitoring and evaluation. Project components are:	2000-2007	695.92 (JBIC-P316.88 m) (GOP P31.08 m) (LGU P347.96 m)	1.80% (Interest rate) 20 years (Maturity period) 10 years (Grace period)	Provinces Identified Ilocos Sur Nueva Vizcaya Occidental Mindoro Oriental Mindoro Palawan Zambales	Cost-sharing in civil works: 36% GOP - 64% LGU (Ilocos) 35% GOP - 65% LGU (NViz) 33% GOP - 67% LGU (OccMin) 38% GOP - 62% LGU (OrMin) 39% GOP - 61% LGU (Palawan) 34% GOP - 66% LGU (Zambales) NG/GOP counterpart includes	Delays have been noted in implementation to the delays in the full mobilization of the Provincial Water Supply Units (PWSUs) and Municipal Sector Liaison Teams (MSLT), the project personnel counterpart from the LGUS. The PWSUs will assist the MSLTs in the selection of sites through the participation of the local commun-

Program/Project Title	Funding Institution	Implementing Agency	Description	Duration	Loan/Grant Amount (In Million Pesos)	Terms and Conditions of Funding Institution	Location	Cost-Sharing Arrangements	Status/Remarks
			a. Construction and development of deep wells, shallow wells and spring development and procurement of materials; b. Construction of school toilets and public toilets; c. Provision of service vehicle, well rehabilitation equipment, maintenance tools and water quality testing kits; and, d. Institutional support consisting of LGU capability enhancement program and community management program for BWSA.					consultancy, institutional development, community organization and training, part of civil works component and part of administrative support. LGU counterpart includes local labor and materials, administrative support, right of way and land acquisition, and cash out-lay for civil works.	ities. Likewise, there is also a delay in the hiring of NGOs who will assist DILG and the Consultant in the site selection.
E. ***Rural Development***									
15 Spanish Assistance and Integrated Livelihood Project (SAILP)	Spanish Government		The project involves the establishment of credit extension, infrastructure support, institutional development and provision of technical assistance. The specific components include: the Camiguin Island Livelihood Program, equipment rehabilitation, cost of housing resettlement, construction of HRD center, improvement of hospital, construction of day care center and waterworks system.		(Forex $3.5 m)	No data available	Province of Camiguin	With subloan component	
16 Aurora Integrated Area Development Project Phase 2	EU	DA	The project is a resouce-based multi-sectoral rural development project whose aim is to assist the rural communities in increasing their production incomes and living standards. The specific components include: agricultural crop production, livestock production, farm-to-market roads, new roads, construction of the Baler Ice Plant and Cold Storage facility and credit micro-projects.	1995-1999	TPC:P648.27 m EU Grant:P543.34 m Local: P104.89 m	Grant	Aurora Province	Provided as gant from NG to LGUs.	Completed.
17 UK-assisted President's Bridge Program	United Kingdom	DILG	The project involves construction of 138 local bridges into steel bridges through the provincial/ city government with about a total length of 4,681.61 lineal meters covering 3,596.6 l.m. single lane bridge and 1,085.03 l.m. double lane bridges.	1996-2000 (to be completed in 2001)	817.26 (Forex $543.69 m) (Local P273.57 m) (Sterling Pounds 13.32 million - original currency)	6.60% (Interest rate)	Nationwide	Provided as grant from NG to LGUs. Reimbursement of up to P500,000 to be given by DILG. Beyond this cost, the LGU will have to shoulder/	Completed 138 bridges.
18 Southern Philippines Zone for Peace and Development (SZOPAD) Social Fund	WB and other bilateral donors	SZOPAD Social Fund	The project aims to increases the access of population in SZOPAD to basic economic and social infrastructure, services and employment opportunities through financing of sub-projects for local initiatives. The Fund provides grant fianncing to LGUs, NGOs and community groups for small-scale social and ecoomic infrastructure, such as rural roads, rural water supply and sanitation, small scale irrigation schemes, health centers, post-harvest facilities and schools. Financing is also available for supplies, equipment, and technical services related to the delivery of community services, such as teaching materials, medical equipment and essential medicines.	1998-2002	WB Loan: $10 m	variable (Interest rate) .75% (Commitment fee) 20 years (Maturity period) 5 years (Grace period)	Provinces/Cities Identified: Luzon - Palawan, Puerto Princesa City Mindanao - Basilan, Zamboanga del Norte, Zamboanga del Sur, Davao Oriental, Saranggani, South Cotabato, Lanao del Norte, North Cotabato, Lanao del Sur, Maguindanao, Sulu, Tawi-tawi, Dipolog City, Pagadian City, General Santos City, Digos City, Kidapawan City, Iligan City, Cotabato City, Marawi City	Provided as grant from NG to LGUs/beneficiaries.	Of the toal 480 approved projects, 461 have been contracted which translates to a contracted of P272.22 M. Of the 461 projects, 416 have been completed P242.7 M), 35 are ongoing (P23.26 M), 7 cancelled (P3.2 M), and 3 are recommended for cancellation (P3 M). Top 5 areas with the most number of complted projects are Lanao del Sur (46); Maguindanao (41); North Cotabato (39); Sulu (33); and Zamboanga del Sur (26). In terms of the types of completed projects, top 5 types of completed projects are warehouse/solar drier (93); madrasah schools (90); schoold bldg. (61); barangay health station (41); and communal toilet/septic tank (28). Primary reason for the cancellation of sub-projects is the unstable peace and order condition in the concerned areas contributing to the unexpended budget of $1.1 million.
19 The President's Bridge Program, Phase II (Austrian-Assisted)	Austria	DILG (Executing Agency) LGUs (Implementing	The project aims to enhance the bridge building capacity of the LGUs through (a) construction of about 303 bridges or 12,025 linear meters of local bridges	1999-2003	4,453.73 (Forex ATS 1 b) (GOP/NG P281. 5 m)	4.5% (Interest rate) 0.125%	Nationwide	Provided as grant from NG to LGUs. Reimbursement of up to P500,000 to be given	Six regional bridge depots were already completed. These are located in La Union, Legaspi City, Iloilo City,

Program/Project Title	Funding Institution	Implementing Agency	Description	Duration	Loan/Grant Amount (In Million Pesos)	Terms and Conditions of Funding Institution	Location	Cost-Sharing Arrangements	Status/Remarks
		Agencies)	nationwide; (b) establishment of regional bridge depots; and (c) training of about 250 national and local engineers in the field of bridge design, erection and maintenance of steel bridges, including riverworks training.		(LGU P1,072 m)	(Commitment fee) 20 years (Maturity period) 9 months after acceptance of Certificate (Grace period)		by DILG. Beyond this cost, the LGU will have to shoulder/	Cagayan de Oro City, Davao del Norte and Tacloban. Construction of the remaining 2 depots in the province of Quezon and Mandaue City are ongoing.
20 The President's Bridge Program, Phase III (UK-Assisted)	United Kingdom	DILG (Executing Agency) LGUs (Implementing Agencies)	The project involves the provision of 402 permanent and maintenance-free double lane bridging materials having a length ranging from 21 linear meters to 64 linear meters. The proposed bridge site should be included among the list of 10 bridges within the province; the barangay location should belong within	2000-2004	6,806 (Forex Loan Pounds 98 m) (Local/GOP P632.13 m)	No data available	Nationwide (except NCR and ARMM)	Provided as grant from NG to LGUs. Provided as grant from NG to LGUs. Reimbursement of up to P500,000 to be given	84 bridges being constructed nationwide while 54 bridges are already completed and open to traffic. The first and second consignment for the bidding materials totalling to
			the 4th to 6th class municipality; and should have the RDC endorsement. The project also aims to (a) enhance the capabilities of the LGUs and facilitate the transfer of technology in the areas of steel bridge planning, design, construction and maintenance; (b) empower LGUS to build barangay bridges as quickly and effectively as possible under DILG direction and supervision; and, (c) hasten people empowerment by enlistung and tapping available labor. The specific components/outputs are: a. Construction of 15,282 linear meters of double lane bridging; and, b. Training of 250 national and local government engineers in the field of Design and Erection of Compact Bridges, as well as the design and construction of substructures.					by DILG. Beyond this cost, the LGU will have to shoulder/	1,815 l.m. and 2,616 l.m. respectively have already been delivered to the first 5 regional depot. Construction of 9 bridges already ongoing while the proposed bridges are under various stages of site evaluation and design.
F. ***Urban Development***									
21 Central Visayas Development Project (CVDP)	Japan/JBIC	DPWH Regional Development Council VII	The project aims to contribute to the nation's economic recovery by promoting the strategy of industrialization, modernization and urbanization. The specific components are: CV Ports Package (under negotiation - P11.5 b) CV Airports Package (under negotiaion - P8 b) Cebu LRT (under negotiation - P10 b) CV Highways Project (under negotiation - P10.16 b) Naga-Toledo Road (PH-P204 - P899.26 m)	1999-2007		1.80% (Interest rate) 20 years (Maturity period) 10 years (Grace period)	Provinces of Central Visayas	Road is provided as grant. LGUs will have to shoulder taxes and right-of-way.	Releases have been made from MDFO for feasibility studies. However no releases have been made for actual projects. The Naga-Toledo Road is a grant from NG to the province.
22 Metro Cebu Development Project, Phase 3	Japan/JBIC	DPWH	The project involves the construction of road segments along the South Coastal Road.	1996-2004	0.614 (For Road Segment 1) 5.938 (For road segments 2 and 3)	2.70% (Interest rate) 20 years (Maturity period) 10 years (Grace period)	Cebu Province	Road is provided as grant. LGUs will have to shoulder taxes and right-of-way.	

Sources: Various reports and documents from DOF-MDFO, NEDA, executing/implementing agencies, and donor country programs.

ANNEX II-C
Grants to Local Government Units for Capacity Building/Technical Assistance Activities
As of end December 2001

Program/Project Title	Funding Institution	Implementing Agency	Description	Duration	Loan/Grant Amount (Million Pesos)	Terms and Conditions of Funding Institution	Location	Cost-Sharing Arrangements	Status/Remarks
A. *Health*									
1 Urban Health and Nutrition Project	WB	DOH (lead/executing), LGUs (implementing)	The project aims to improve the health and nutritional status of urban slum women, their children and families; build capacity of city and municipal governments in these areas to plan, finance and implement cost-effective slum health and nutrition programs, and help the DOH improve outreach and cost-effectiveness of health and nutrition delivery systems. The components are: a. Service delivery - TB component, Integrated Maternal and Child Health; b. Capacity building; c. Community partnership for health; and, d. Policy research and evaluation.	1994-2001	(Forex $47.2 m)	Variable (Interest rate) 25 years 3/4 of 1% (Commitment fee) 25 years (Maturity period) 5 years (Grace period)	17 cities in NCR, Mandaue City, Lapu-lapu City, Cebu City and Cagayan de Oro City	Provided as grant by NG to LGUs.	Notable improvements in the DOH procurement system has resulted in the reduction in bid prices for TB drugs by 40% compared to to DOH procurement for TB drugs in December 1998 suggesting that the DOH has successfully been able to apply competitive bidding procedures, DOTS firmly in place in the LGUs, and the involvement of Apex NGO under the revised project resulted in the implementation of 59 successful community projects and helped build useful partnerships among LGUs, communities and local NGOs.
2 Street Children Nutrition and Education Project	AusAID	DILG	The project involves the provision of 7,845 metric tons of wheat flour by Australia to be sold in the Philippines through the supervision of the World Food Program. Proceeds from the monetization will be used to purchase local rice which in turn, will be provided to about 7,000 street children and their parents in 10 cities as an incentive to encourage them to have a better lifestyle. Project components are: a. Rice assistance and services; b. Social Development Centers (SDCs) for each of the 13 participating LGUs; and, c. Livelihood component for parents of the street children.	1994-2001	298.80 (Forex $4.06 m) (Local P136.4 m)	Grant	Baguio City Angeles City Olongapo City Iloilo City Bacolod City Cebu City Cagayan de Oro City Davao City City of Manila Caloocan City Quezon City Makati City Paranaque	LGUs to provide land acquisition, ROW for the component of the social development center.	
3 Integrated Family Planning and Maternal Health Program	USAID	DOH	The program is a seven-year project, national in scope, with the development objective of reducing the unmet need for family planning and selected child health services. It aims to (a) expand the availability of reproductive health services in the public and private sectors and to increase use of three services by women in high risk groups; and (b) foster continued provision of selected child health intervention at the LGU level. The program's components are: a. LGU Performance Program - performance disbursement and program management for 75 LGUs b. National services - national systems strengthened to promote and support family planning and maternal child health; and, c. NGO/private sector increased private sector provision of family planning/maternal child health services.	1994-2002	3,107.50 (Forex $90 m) (Local P857.5 m)	Grant	98 LGUs in 16 regions	Provided as grant from NG to LGU.	For the LGU Performance Program, only 63% of the LGUs passed the benchmarks for the program. As a result, the 7th tranche release was also reduced to 63% of the original amount, from $6.6 million to $4.158 million.
4 Women's Health and Safe Motherhood Project	Kreditanstalt fur Weideraufbau (KfW) WB ADB	DOH	The project aims to improve the health status of women, particularly those of reproductive age by improving the quality and range of women's health and safe motherhood services; strengthening of LGUs to manange the provision of such services; and of the DOH to provide related policy, technical; financial and logistical support. It also aims to enhance the effectiveness and sustainability of health interventions through the participation of local communities and NGOs and expanding the knowledge base up on which to draw policy and technical guidance for women's health peograns.	1995-2001	KfW: $14.23 m ADB: $54 m WB: $13.7 m	6% of CQB (WB interest rate) 3/4 of 1% of undisbursed balance (WB Commitment fee) 15 years (WB maturity period) 5 years (Grace period) KfW: provided as grant Variable (IADB nterest rate) 25 years (Maturity period) 1% (service charge) 5 years (Grace period)	77 provinces nationwide	Provided as grant to LGUs.	Procurement of all goods under KfW is already 100% complete but delivery stands at 93%. Major gynaecological and obstetrical equipment worth $13.5M has been delivered to 86 provincial and district hospitals. There are still 6 hospitals with incomplete civil works for which equipment have to be delivered in order to complete the targeted 92 hospitals under the project. Midwifery and TBA kits in support of AusAID and HMDTS Training have been delivered since May 1999 in time with the training schedule. About 41 units of ultrasound machine have been delivered to the 41 ADB provinces after the training sessions. RTI/STD drugs will be delivered in 3 batches (since Sept 1999). The1st 2 batches has been completed and had been delivered to the 10 RTI provinces. The 3rd batch will be distributed thru the 16 DOH regional

Program/Project Title	Funding Institution	Implementing Agency	Description	Duration	Loan/Grant Amount (Million Pesos)	Terms and Conditions of Funding Institution	Location	Cost-Sharing Arrangements	Status/Remarks
									health offices which were given the responsibility of determining which province the drugs will be distributed.
5 Family Planning and Maternal and Child Health Project Phase II	JICA	Department of Health	The program seeks to disseminate the gains from the Family/Maternal Child Health Project in Tarlac to the rest of the provinces in Region 3 in order to achieve region-wide improvements in reproductuve health status. The specific components are: a. Improvement of FP/MCH service delivery in 221 rural health centers/5 provinces; b. Reinforcement of community health activities; c. Capacity building for health workers in the entire region; d. Establishment of a monitoring and evaluation system; e. Health promotion through IEC; f. Development of linkages between Phase I and Phase 2 implementors; g. Strenthening of LGU involvement in 6 provinces; and, h. NGO collaboration.	1997-2002	132.40 (Forex $5.03 m)	Grant	Provinces Identified: Bataan Bulacan Nueva Ecija Pampanga Tarlac Zambales		The number of trainings include 9 local and 2 overseas, where a total of 188 persons benefitted. For IEC, 2 videos were produced on adolescent reproductive health and on general health. For research and development, an evaluation study of project activities was done.
6 Women's Health and Safe Motherhood Project Partnerships Component	European Union AusAID	DOH	The project aims to improve the health status of women by supporting partnership activities geared towards empowering women and communities to improve their health conditions and preferences. The components are: a. IEC/Advocacy; b. Capacity building; c. Community health care; and, d. Community-based health actions.	1997-2002 (EU)	EU: $13 m AusAID: $10.6 m	Grant	Provinces Identified: Abra, Benguet, Ifugao, Mt. Province, Albay, Camarines Norte, Camarines Sur, Masbate, Sorsogon, Biliran, Northern Samar, Western Samar, Northern Leyte, Southern Leyte, Bukidnon, Misamis Oriental, Misamis Occidental, Agusan del Norte, Agusan del Sur, and Surigao del Sur.	Provided as grant from NG to LGU.	The project is being implemented in all five regions. It has established 6 project offices and a network of partners, at village, municipal, provincial, regional and national levels. Also established were 200 women's organizations now implementing 2,224 micro-projects. Implementation is ongoing for community health care, capacity building, advocacy and women's health action in 159 villages in 5 regions. The project has also conducted KAP surveys and other research on women's issues including Violence against women, women's and children's rights. The project also supported the First Safe Motherhood Congress that produced a framework for developing community-based referral system.
7 Integrated Community Health Services Project	AusAID	DOH	The project aims to improve the effiency and effecetiveness of the health care delivery system through a comprehensive approach to health system developnent at a local level by providing support for health systems development in two Mindanao provinces and community development in the six provinces of the project. The components are: a. LGU Health Management System b. Health referral and delivery c. Community and NGO mobillization.	1997-2003	(Forex $14 m)	Grant	Kalinga, Apayao, Palawan, Guimaras, Surigao del Norte, South Cotabato	Provided as grant from NG to LGU considering the component.	Delays have been experienced in such critical areas such as continued refinement of and development of key local health systems, preparation and implementation of the Replication Plan, health promotion and procurement. To address the issues, the DOH has created a Management Team to undertake hands on supervision of the day to day management of the ICHSP-PMO. This team shall carry on its assignments until the ICHSP-PMO has been strengthened.
8 Family Health by and for Poor Settlers (FAMUS)	German Technical Cooperation Agency (GTZ)	DOH (Executing Agency) LGUs (Implementing Agencies)	The project, through DOH, mobilizes LGUs to invest through NGOs towards (a) improvement of family health self-management capabilities and the increase in the utilization of family and reproductive health by target groups; (b) the organization and support of the community centers for family health in the villages and (c) family health workers development.	1999-2001	(Forex DM 4.3 m)	Grant	Provinces Identified: Cavite Quezon Agusan del Norte Bukidnon Misamis Oriental Agusan del Sur Surigao del Sur Quirino Cebu Negros Occidental	LGUs provide counterpart personnel, office space and MOOE. The German contribution is in the form of services, basic office and commu-nication equipment.	MOAs with partner LGUs have been prepared.
9 Social Health Insurance Networking and Empowerment (SHINE)	GTZ	DOH and PHILHEALTH	The project supports the implementation of an efficient and equitable health insurance system in the Philippines. Technical assistance provided to the LGUs are the following: a. Health Insurance Management Information Systems	1999-2003	(Forex DM4.5 m)	Grant	Bukidnon Guimaras	At the national level: PhilHealth provides office space, utilities and stationeries. The LGUs provide the hardware for	The Mgt Info System (MIS) running in both LGUs and are being maintained. IEC tools in the process of being refreshed and complemented by additional tools. Training modules on social health

Program/Project Title	Funding Institution	Implementing Agency	Description	Duration	Loan/Grant Amount (Million Pesos)	Terms and Conditions of Funding Institution	Location	Cost-Sharing Arrangements	Status/Remarks
			(MIS) (software development); b. IEC tools to promote social health insurance; c. IEC training on social marketing as a tool to promote social health insurance; and d. Facilitation activities to interface mechanisms between the PhilHealth and the Provincial Government of Bukidnon.					the software developed by the SHINE project. Some cost-sharing arrangements regarding transport costs during visits.	insurance promotion being developed. Cooperation, interfacing or integration schemes between LGUs (and other groups) and PHIC being developed on a broader scope than only with the LGU.
10 Fifth Country Program for Children	UNICEF	NEDA, DSWD, DOH, DECS, NNC, DOLE, DOHJ, DILG, PIA, FNRI, CWC, CHR, NSO	CPC V aims to contribute to the attainment of the Filipino vision and goals of the proposed Philippine National Development Plan for Children. The program aims to achieve the following objectives: (a) strengthen national and local governments' capability to implement the CRC; and, (b) contribute to massive mobilization in support of a child-friendly movement at all administrative levels, local communities and within the family. The program strategy focuses on the transformation of the CRC from a legal framework into a well-defined, nationwide Child-friendly movement (CFM) involving the families, communities, local and national governments, as well as the private sector.	1999-2003	(Forex $46.50 m)	Grant	Model building and direct service delivery in 20 provinces and 5 cities: Mt. Province, Isabela, Manila, Pasay, Quezon City, Aurora, Camarines Norte, Masbate, Antique, Guimaras, Capiz, Negros Oriental, Cebu City, Eastern Samar, Northern Samar, Zamboanga del Sur, Bukidnon, Saranggani, Davao City, Sultan Kudarat, North Cotabato, Agusan del Sur, Maguindanao, Sulu and Tawi-tawi.	LGU share is the payment of taxes and duties.	The project is still in the advocacy and training stage to promote a child-friendly environment. The activities that have been undertaken are: Under Creating Child-Friendly/Learning Conditions for Education for All are mainly on meeting the basic learning needs of families and building support and sustainability for child friendly schools. This include advocacy to teacher training institutions, technical assistance to the division of Bukidnon and pilot child friendly shools; various orientations, trainings and workshops; and risograph reprinting of the revised 8-week curriculum for CPC V provinces which are non-Early Childhood Development Project (ECDP) provinces. On Health and Nutrition, sub-programs include, maternal health and nutrition, child health and nutrition and micronutrient deficiencies control which undertook activities such as development of IEC materials, development of food fortification strategies, training on various maternal and child health interventions. Other ongoing activities are on gender and development, local policy and institutional development, children in need of special protection and communication.
11 Street and Urban Working Children Project (SUWCP)	AusAID/Vulnerable Groups Facility	DILG-Food for Work Project Office	The project is a three-year Vulnerable groups facility-assisted project which aims to support national and local initiatives in addressing various concerns of the street and urban working children in the country. An appropriate package of assistance for SUWC and their parents, as well as for partner implementers have been developed, to strengthen the local capacity to plan and provide services to its constituents. Specifically the project entails the provision of rice as an incentive to street and urban working children and their parents, to motivate and encourage them to avail of educational and training opportunities, and social services being provided by LGUs, NGOs and GOs. It shall also provide funds for the purchase of school supplies and rice carry bags for SUWC beneficiaries and for the constuction and equipping of SDCs as well as livelihood funds for the income-generating projects of the parents of SUWC.	2000-2002	238.8 m (AusAID) 36.9 m (GOP) (Forex: A$9.55 m)	Grant	Baguio, Angeles, Olongapo, Naga, Legaspi, Bacolod, Iloilo, Cebu, Lapu-Lapu, Mandaue, Zamboanga, Cagayan de Oro, Davao, General Santos, Cotabato, Quezon, Manila, Makati, Caloocan, Paranaque, Pasig, Pasay, Las Pinas, Mandaluyong, Muntinlupa	LGU counterpart may be in the form of in kind contributions.	School supplies amounting to P3.3 m have been released to street children beneficiaries under the formal and non-formal education component. In terms of beneficiaries, a total of 23,033 street children, 11, 927 parents and 276 volunteers covering 24 out of the 25 participating cities (Paranaque not included) have been served.
B *Agriculture and Agrarian Reform*									
12 Low-Income Upland Communities Project	ADB	DENR, LGUs and NGOs (Implementing Agencies)	The project is in partnership with LGUs and NGOs to address, in a pilot and integrated approach, sustainable upland socio-economic development through self-reliance and the provision of improved government services such as provision of security of tenure, improved agroforestry technologies, adoption of diversified income generating activities, easy market access, education, health and other basics. To accelerate the sustainable development and management of critical watersheds with and through the cooperation of the upland communities, particularly tribal groups. The components are: a. Community Organization and Cooperatives Development; b. Resource Access and Resource Management; c. Agroforestry, Reforestation, and Livelihood; d. Infrastructure and Social services; and,	1990-1999	TPC $34.35 m (Forex $26.35 m) (Local $8 m)	Grant	Oriental and Occidental Mindoro	Grant from NG to LGU.	The project was completed on 31 December 1999. Phase In/Out Plan indicates that the LGUs are responsible for maintenance.

Program/Project Title	Funding Institution	Implementing Agency	Description	Duration	Loan/Grant Amount (Million Pesos)	Terms and Conditions of Funding Institution	Location	Cost-Sharing Arrangements	Status/Remarks
			e. Project management and institutional building.						
13 Farm Integrated Animal Health and Production Program	German Government through GTZ	DA-Bureau of Animal Industry	The project aims to assist the LGUs and NG in the implementation of specific interventions for animal health and production program.	1991-2001	299	Grant	5 Provinces and 34 municipalities: Albay - Daranga, Guinobatan, Legaspi City, Ligao, Malilipot, Malinao, Polangui, Tabacco, Tiwi. Bulacan - San Ildefonso, San Rafael, Guiguinto, Plaridel, Calumpit. Cagayan - Iguig, Penablanca, Solana, Tuguegarao. Camarines Sur - Canaman, Libmanan, Milaor, Minalabao, Nabua, Naga City, Pamplona, Pili, San Fernando, Sipocot. Laguna - Cavinti, Magdalena, Pagsanjan, Sta. Cruz.	GOP/LGUs provide pesonnel services and office MOOE.	Completed in June 2001. LDTTRF, a foundation and private partner of FIAHPP shall continue the livestock services to the covered areas to sustain the FIAHPP approach and plan to expand to other areas.
14 Small Islands Agricultural Support Services Program	EU	DA	The project aims to assist rural communities to initiate and sustain increases in output from farming and fishing through the following strategies: a. Improvement of rural production and productivity in such sectors as agriculture, livestock and fishery; b. Improvement of market access and development of market opportunities; c. Strengthening of institutional capabilities for sustained development, particularly farmers' and fishermen's organizations, cooperatives and LGUs; and, d. Assurance of environmental sustainability by arresting environmental degradation and introducing sustainable management practices.	1994-1999	697.5 (Grant P620 m) (GOP P77.5 m)	Grant	Location/Site: Zone 1 - Guimaras - Municipalities of San Lorenzo, Sabunag N. Valencia, Jordan and Buenavista. Zone 2 - Biliran, Leyte - Municipalities of Calaba, Naval Almeria, Cabucgayan, Kawayan, Caibiran, Maripipi, Biliran. Zone 3 - Islands of Bantayan, Camotes and Pitogo, Cebu Municipalities of Bantayan, Madridejos, Santa Fe, Pilar, Poro, San Francisco, Tudela and Pitogo.	Grant from NG to LGUs.	After completion of EC assistance in March 1999, GOP, through the DA, continued to fund a SMISLE Exit Plan until December 1999. Activities undertaken under this Plan included provision of support in the implementation of sustaining mechanisms and training activities to address the concerns on capability building of both the LGUs and the communities and ensure quality of community exit process especially for the communities which did not complete the process. The SMISLE experience showed that a 5-year project life is not sufficient for the achievement of the project objectives through the implementation of a community-driven development process which is complex and time consuming because of the participatory process involved. The failure to extend the project, particularly after indications fom EC of possible extension, meant that commitments in some communities were pre-terminated to the detriment of sustainability and loss of credibility for the donor and the executing agency.
15 Western Samar Agricultural Resources Development Program (WESAMAR)	EU	DA	The project aims to alleviate poverty and promote sustainable socio-economic development through an integrated area based development directed towards the concerns of the rural poor. The major components are: a. Organizing and capability-building of communities; b. Strengthening of LGUs front-line service teams with provision for additional skills and resources; c. Conservation and managerial inputs for critical eco-systems; d. Provision of credit, infrastructure and technical support to farm and fisheries activities of community organizations; e. Provision of training and livelihood support to community organizations; f. Integration of the bias for women's participation in community activities; g. Provision of support to local agrarian reform activities; and, h. Provision of support to management and delivery of health services.	1994-2000	609.85 (Grant P547.74 m) (GOP P62.11 m)	Garnt	Province of Samar - Municipalities of Pagsanhan, Tarangana, Catbalogan, Talabon, Daram, Zumarraga, Jiabong, Motiong, Paranas, Hinabangan, San Sebastian, Calbiga, Pinabacdao and Villareal.	Components/Activities with cost-sharing: a. Conservation and managerial inputs for critical ecosystems - 90% DA, 10% CBO counterpart. b. LGU initiated projects 70% DA, 30% LGU c. Grant infrastructure program activities 80% DA, 20% from Brgy IRA and CBO counterpart. d. Technical support to farm and fisheries activities of community organizations 90% DA, 10% CBO counterpart.	The project was not able to implement some of its targeted activities and outputs due to delays in the approval of the Rider agreement for the project's extension which led to delayed fund replenishments. Major accomplishments to date are as follows: 1. In the Community and Institutional Dev't. component, 300 community-based org. (CBOs) have been organized from 164 brgys. and 14 mun. A total of 470 microprojects have been implemented by the CBOs benefitting over 7,000 households. 2. Under the macro-enterprises, joint venture companies of CBOs, NGOs and other baywide cooperatives have been established and have ventured into WESABOAT, which manufactures fiberglass boats and WESAMARINE, which operates a multi-specie hatchery. Marine enterprises I.e., eucheuma, lapu-lapu and tilapia fish cages and a pearl farm are being aggressively implemented; and 3. A Bay-wide Management Council has been established for the protection and rehabilitation of Maqueda Bay, by the Local Chief Executives in partnership with local NGOs and other concerned agencies.

Program/Project Title	Funding Institution	Implementing Agency	Description	Duration	Loan/Grant Amount (Million Pesos)	Terms and Conditions of Funding Institution	Location	Cost-Sharing Arrangements	Status/Remarks
16 Central Cordillera Agricultural Programme, Phase II	EU	DA	The project aims to promote a self-sustaining improvement in the living condition for rural communities in the Central Cordillera. It is a continuation of CECAP Phase I and will emphasize a community-based participatory approach. CECAP Phase II aims to increase income and strengthen resource management capabilities of rural households in 25 municipalities of the Central Cordillera through the implementation of interventions in agriculture, natural resource management, infrastructure, marketing and enterprise development, rural finance and institutional development.	1996-2003	1,100 (Forex EURO 23 m) (Local P180 m)	Grant	25 municipalities in Central Cordillera	Grant from NG to LGU.	In all municipalities, the growth in the number of clients for the savings and loan has been impressive in the 200 barangay sites; 1 in 4 households have joined in the Savings and Loan Groups and or Producer's Group members. In other municipalities the ratio is 1 to 2; while the average is not lower than 1 in 8. Approved projects in infra directly or indirently benefitted 19,000 households.
									The Natural Resources Management component has 160 ongoing projects while the Marketing and Enterprise Development has over 30. The program has also made good progress in identifying and strengthening farmers organizations which will continue to provide credit and marketing services after CECAP. A large number of Village Water Systems and irrigation systems are about to be completed and attention will shift more to assistance to associations which will use and maintain them. Main LGU attention is focused on an expanded road rehabilitation and maintenance programme, but good progress has been achieved as well in cooperation on agricultural extension and veterinary services.
17 Support to Asset Reform through the Comprehensive Agrarian Reform Program (SARDIC) and Development of Indigenous Communities	UNDP	DAR	The project intends to undertake an array of activities which will result in (a) policy development and advocacy in support of agrarian reform measures; (b) establishment of local agricultural extension development plans; (c) training of extension workers and provision of extension facilities; (d) creation of a network system of extension and support organization; and, (e) organizational development productivity enhancement and market and	1997-2001	148.03 (Forex $3.20 m) (Local {18.66 m)	Grant	Provinces Identified: Capiz Iloilo Western Samar Davao del Sur Lanao del Norte North Cotabato	No cost-sharing since the LGU component is for training/capability building.	Project has been extended from 2000 to December 2001.
18 Cordillera Highland Agricultural Resources Management (CHARM) Project	ADB IFAD	Department of Agriculture (DA-Executing Agency) with NIA, DAR, DENR, Provincial Governments of Abra, Benguet and Mt. Province.	The objective of the project is to reduce poverty in the Cordillera Administrative Region by increasing the disposable incomes of small farm-holder families in the target area. This will be achieved by training and participation involving target communities to improve resource management practices, including reforestation. The specific components/activities are: a. Community Mobilization and Resource Management; b. Rural Infrastructure Development (Farm-to-market access, community irrigation, domestic water supply) c. Agricultural Support Services (agribusiness services, extension services, adaptive research, rural financial services, integrated pest management); and, d. Project Management and Coordination (project management, planning, monitoring and evaluation, GIS, administrative and financial services, information and training).	1997-2003	1,452.00 (Forex $35.6 m) (Local P248 m; LGU counterpart is $3 m & beneficiary contribution is $2.4 m)	Variable (interest rate) 0.75% (Commitment fee) 20 years (Maturity period) 5 years (Grace period) IFAD: 0.75% interest rate 40 years (Maturity period)	**Abra** - Municipalities of Boliney, Bucloc and Salapadan **Benguet** - Municipalities of Atok, Bakun, Bugulas, Kapangan, Kibungan, Sablan, Tuba and Tublay **Mt. Province** - Municipalities of Bauko, Bontoc, Sabangan, Sagada and Tadian	In terms of TPC: DA - 19% LGU - 7% Others - 74% broken down as follows: ADB - 46% IFAD - 22% Beneficiaries - 6%	Satisfactory performance noted for the project. However the issues are: 1) slow utilization of and liquidation of funds transferred to other participating agencies; 2) lack of cash to replenish increased fund requirement for infra projects; 3) unavailability of LGUs and beneficiaries to provide sufficient counterpart funds; and 4) redefined role of DENR, DAR and NCIP as a result of the final IPRA affirmation by the SC.
19 Caraballo and Southern Cordillera Agricultural Development Programme (CASCADE)	EU	DA	The specific components and/or sub-projects implemented are: a. Agricultural Production Systems - farming systems development; agricultural support services; marketing systems program; and group strengthening program; b. Micro-enterprise development - vocational training program; micro-enterprise training program; product development program; c. Social development - nutrition program; potable water supply program; waste management and sanitation; basic health services program; d. Institutional development - strengthening of LGU planning; other support to LGUs; strengthening of local development councils; natural resources management by LGUs; e. Rural finance - micro-finance system development; and cooperative credit support program.	1997-2004	Total: Euro 22.5 m (Forex: Euro 13.5 m) (GOP: Euro 4 m) (LGUs: Euro 3.5 m) (Beneficiaries: Euro 1.5 m)	Grant	Provinces Identified: Nueva Vizcaya Benguet Nueva Ecija	DA - 18% LGU - 16% EU Grant - 60% Beneficiaries 6 % Provincial and Municipal LGUs provide equipment and technical staff. Beneficiaries provide labor and local resources. Project provides financial support.	The eview and approval of infrastructure proposals are on schedule but the implementation is slightly delayed due to dexceptionally rainy periodsin the first half of 1999, unavailability of LGUpartners due to other pressing concerns anddelayed compliance to pre-implementationconditions and problems experienced on thedesign of some infrastructure projects. Major accomplishments are as follows: a) Institutional Development - an IP's Mission was undertaken which will serve as guide to further harmonize the working relations between the project and the IPs. The community planning methodology has been improved to incorporate Barangay

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									Resources Assessment in the formulation of Barangay Development Plans; b) Microfinance - 150 savings and loan groups formed with a total accumulated savings of P319,568; and c) Agricultural Production and Marketing - assessment/inventory of existing and potential irritation systems in the project area was undertaken and training of 375 farmers and 10 agricultural technicians on Integrated Pest Management. There is also an ongoing assessment of Production and Marketing Analysis Service and the Agricultural Marketing Info Systems with BAS, CHARMP and CECAP.
20 Upland Development Programme in Southern Mindanao	EU	DA	The project aims to develop and test a replicable model for sustainable management of the natural resources in the uplands of five provinces in Region XI; and to enable the communities to address their subsistence needs and to produce new marketable surpluses through sustainable market-led agricultural development. The specific components/activities are: a. Sustainable Agriculture Development; b. Resource Management; c. Marketing and Enterprise Development; d. Rural Financial Services; e. Community Development, Institutional Development and Extension; and, f. Agricultural Extension Support.	1998-2005	1,678.43 (Grant P631.35 m) (GOP P264.96 m) (LGU/PFI P350.18 m) (Beneficiaries P431.94 m)	Grant	Southern Mindanao	DA - 15.79% LGU - 19.73% Others - 64.48% broken down as follows: EU Grant - 37.62% Beneficiaries - 25.73% Partner Financial Institutions - 1.13%	The Community andInstitutional Development and Extension(CIDE) component focused on the establish-ment and strengthening of the sitio-basedUpland Barangay Organizations (UCOs) andthe cluster-based Upland Barangay Assoc.(UBAs) of the 1st barangays and the initialorganizing of the UCOs and UBAs among the2nd barangays after the completion of theformulation of the community watershedplans at the sitio and at the cluster level inthese barangays. The Resource Management Component has significantly progressed in its key result areas for the realization of its overall objective which is the development of a model for sustainable management of the natural resources in the upland by the communities particularly in the first 60 barangays that are covered by the Programme since last year. For the Sustainable Agriculture Develop-ment component, 110 Agro-Ecological Zone (AEZ) and Production Base, crop inventory/matching were conducted, most of which are in the 2nd barangay sitios for all 5 provinces. A total of 1,621 farm plans were formulated and undergoing validation, 315 of which were already approved. The cooperation with the LGU's was given a boost by the implementation of the Farming System Modelling activities where the LGU teams pledged their resources together with the inputs from the Project. During the cul-mination of the farming system seminar, fruit tree seedings and even livestock were among the commitments of the LGU teams. The Rural Financial Services component has started to conceptualise the Financial Ser-vice Center (FSC) as the envisioned financial services system at the barangay level, with the launching of the first FSC to be granted a P100,000 Seed Capital Fund (SCF) in Palo 19, Tampakan, South Cotabato.
21 Western Mindanao Community Initiative	IFAD	DAR	The project provides financing for community and institutional development resource management for small enterprise and credit to increase subsistence in cash crops and fishery production and increase income of about 16,000 farma nd fisherfolk households in selected areas in Region IX. The components are: a. Community and institutional development - community organizational development; LGU capacity development (871 municipal/barangay LGUs cadres envisioned to be trained); line agencies processes support;	1999-2004	678.31 (Forex $14.79 m) (Local P100.11 m)	0.75% (Interest rate) 40 years (Maturity period)	Provinces Identified: Zamboanga del Norte Zamboanga del Sur Basilan	Provided as grant from NG to LGU.	Disbursement has yet to be made. Finalization of credit guidelines, sub-financing agreement and promisory note between LBP and Lead Credit Conduits and MOA between LBP and DAR is ongoing.

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			b. Resource management - land resource management, marine/water resource management and infrastructure and resource enhancement; c. Small enterprise development and credit - business advisory services; enterprise development lending;						
22 Fisheries Resource Management Project	ADB and Japanese Government through JBIC (then OECF)	DA-Bureau of Fisheries and Aquatic Resources	The project is envisaged to address the critical issues of fisheries resource depletion and persistent poverty among municipal fisherfolk. The project will establish and implement a set of fisheries resource management systems, promote income diversification for municipal fisherfolk, and strengthen the institutional capacity of the public agencies in charge of fisheries resource management, including those at the national, regional and local levels. The project will focus on the nearshore or municipal fisheries sub-sector and will cover 18 out of the 26 priority bays in the Philippines. Components include: a. Fisheries Resource Management; (i) Data management/Philippine Fisheries Information Systems (ii) RCM Planning and Implementation (iii) Fisheries Legislation and Regulations (iv) Community-based Law Enforcement (v) Monitoring, Control and Surveillance b. Income diversification; and, (i) Community Organizing (ii) Promotion of Microenterprises (iii) Support for Mariculture Development c. Capacity building.	1998-2004 (ADB) 1999-2007 (JBIC)	4,567.93 (Loan: P1,662.93 m) (GOP: P2,905 m)	Variable (ADB interest rate) 1.70% (JBIC interest rate) 25 years (ADB maturity period) 35 years (JBIC maturity period) 5 years (ADB grace period) 10 years (JBIC grace period)	Calauag Bay, San Miguel Bay, Tayabas Bay, Ragay Gulf, Lagonoy Gulf, Sorsogon Bay, Carigara Bay, San Pedro Bay, Ormoc Bay, Sogod Bay, Panguil Bay, Honda Bay, Puerto Princesa Bay, Davao Gulf, Lingayen Gulf, Gingoog Bay, Butuan Bay and Sapian Bay. Provinces Identified: Agusan del Norte Aklan Camarines Sur Capiz Catanduanes Davao del Norte Davao Oriental Davao del Sur Lanao del Norte La Union Leyte Misamis Oriental Palawan Pangasinan Quezon Samar Sorsogon Southern Leyte Zamboanga del Sur	Cost-sharing in terms of TPC: DA - 19% LGU - 23% Others - 58% broken down as follows: ADB-ADF - 16% ADB-OCR - 20% JBIC - 22%	Physicalperformance has been satisfactory. Of the total 100 municipalities targettedby the project, 93 municipalities have sofar signed MOAs. Institutional arrangements for project implementation have been established. Activities relating to community organizing, resource and social assessment, and information, education and communication program are ongoing in most of the priority bays. Some of the resource management activities have been initiated in the project areas. With the engagement of the JBIC component team of consultants, work on MCS, licensing and pilot-testing of ICRM are now in full swing and have brought the project in full operation.
C. ***Natural Resources and Environment***									
23 ENR-Sectoral Adjustment Loan Program - Regional Resources Management Component	WB	DENR	The component aims to support the institutional capabilities of LGUs and communities to plan, generate and service small-scale community-based resource management and livelihood sub-projects in upper watershed areas. The specific components are: a. Local social development/community organizing-community development; b. Development of livelihood options; c. Community resources development - provision of tenurial rights to land and natural resources, the development of forest and land resources-base through forest rehabilitation and introduction of sustainable land-use practices; d. Infrastructure and facilities development - barangay development units, multi-purpose bldgs., school buildings, housing units, pavements, roads and bridges construction and rehabilitation, domestic water supply systems and irrigation systems; and, e. Institutional strengthening - development of the capabilities of DENR, LGUs and other concerned government agencies, community associations, and NGOs.	1991-1999	TPC: $54.6 m (Forex $39.08 m) (Local $15.52)	No data available.	Ilocos Sur, Ilocos Norte, La Union, Pangasinan, Nueva Vizcaya, Quirino, Cagayan, Isabela, Batanes, Palawan, Rizal, Negros Occidental, Negros Oriental, Cebu, Bohol, Western Samar, Eastern Samar, Northern Samar, Zamboanga, Basilan, Tawi-tawi, Bukidnon, Misamis Oriental, Misamis Occidental, Agusan, Surigao del Norte, Benguet, Ifugao, Kalinga, Apayao, Abra and Mt. Province.	Each LGU is expected to allocate funds (from IRA) for the sustainability of project interventions and replication of RRMP activities in other areas.	The management responsibility for the RRM component was turned over to the LGUs in 1995. DENR continues to provide technical assistance to RRMP sites. Majority of the LGUs are constrained to provide funds for sustainability and replication. The project was completed on 31 December 1999. The Phase In/ Out Plan indicate the responsibility of LGU to provide support for the maintenance of the infrastructure component and equipment turned over to them.
24 Philippine-German Community Forestry Project - Quirino (Phase II)	German Government GTZ and KfW	Forest Management Bureau (implementing agency)	The project aims to conserve and protect the forest within the project area through sustainable management practices and through community organization and self-help. It main strategy is to facilitate the rural people's organization in planning, mobilizing resources, implementing, monitoring local resources and implementing, monitoring and evaluating the community-initiated natural resource management programs. It also aims to support institutional strengthening of partner organizations, these are, DENR, LGUs, NGOs, financial insitutions, to sustain the project efforts in the area and replicate them on other areas. The components are: a. Land tenure investment; b. Agriculture/agroforestry;	1997-2001	TPC-$8.59 m GOP $1.03 m Total loan or grant proceeds $7.56 m	Grant	Project sites: Municipality Nagtipunan Quirino Brgy Asaclat, Anak; Municipality of Diffun Brgy Baguio Village, Don Mariano Perez; Municipality of Maddela Brgy Villa Agullana	LGUs provide counterpart personnel, office space and MOOE.	Phase I was undertaken from 1992 to mid-1997. KfW component is being implemented from 1994 to 2001.

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			c. Community forestry; d. Land use planning/natural resources management; e. Community-implemented infrastructure; and, f. Rural financing.						
25 Quirino Community-based Forestry Program: A Debt-for-Nature-Swap Initiative	KfW	DENR-PENRO and Provincial Government of Quirino (joint implementing agencies)	The project involves planning and implementation of measures for the protection of the environment and sustainable use of natural resource base with emphasis on biodiversity conservation. The components are: a. Support to community organization activities; b. Participatory land use planning; c. Forest management and biodiversity conservation; and, d. Sustainable agriculture/agroforestry.	1998-2002	TPC: $2.69 m GOP - none Total loan or grant proceeds $2.69 m	Grant	Quirino Province - 10 barangays in the municipalities of Maddela, Nagtipunan, Aglipay and Diffun.	LGUs provide counterpart personnel, office space and MOOE.	The DENR-PENRO and Provincial Government will jointly implement the Debt-for-Nature Swap Program. This is linked to the Community Forestry Project-Quirino in its implementation. Hence, the management of the community forestry project shall assist the PENRO and Provincial Government in the program implementation by providing technical
26 Natural Resources Management Program II - Industrial Initiatives for a Sustainable Environment	USAID	DENR and DTI (Implementing Agencies)	The project aims to promote the spread of cleaner production/environmental management in coastal industries. The project supplements other USAID ongoing natural resources/environmental program	1998-2002	(Forex$8.17 m) (Local $1.01 m)	Grant	Cebu Negros Oriental Bohol Davao del Sur	Provided as grant from NG to LGU.	
			initiatives and builds on the completed Industrial Environmental Management Project. The activity provides technical assistance to the concerned national government agencies, local government units, NGOs, business organizations and trade associations to strengthen their capabilities to advocate for cleaner technology in industries along the selected coastal areas. The components are: a. Area assessment and analyses; b. Integrated environmental management advocacy; c. Local investment packages for environmental infrastructure; d. Institutionalization of cleaner production/environmental management; e. Reduction and prevention of marine pollution; and, f. Support services for promotion of cleaner production/ environmental management.				Saranggani South Cotabato Batangas Palawan Tawi-tawi		
27 Strengthening Local Governments Environmental Planning and Management (LOCAL EPM)	UNDP	DENR (Executing Agency) League of Cities, DILG and Local Government Academy (Implementing agencies)	The project focuses on nurturing and strengthening capacities for urban environmental management and planning at the local level, particularly in secondary cities, and on enhancing the capacity of national institutions to support LGUs. The project aims to (a) strengthen LGUs and their ability to function effectively in the protection of the environment as the basic units of local governance; and (b) enhance LGU capacities for participatory planning and management thereby fostering an equitable and sustainable development.	1998-2005	TPC $2.58 m Forex $2.18 m Local $.4 m (kind)	Grant	City of Lipa (Batangas) City of Tagbilaran (Bohol) City of Cagayan de Oro (Misamis Oriental)	LGUs provide their participation on capability building activities; counterpart funds for demonstration sites; and initiate the formulation and implementation of environmental policy.	The DENR has shown through the conduct of the Local EPM project a capacity to administer a collaborative and process-oriented project involving key development players such as the LGU, LCP, DILG, NGO,, PO, and the business sector. The project has proved thatthrough broad base approach in EPM, theformulation of environmental managementstrategies and actions plans and their operationalization, has extended support tothe three LGUs and their local partners todevelop and strengthen their EPM capabilities.However, the task of defining suitablemechanisms and structure within each of thedemonstration city that could sustain theEPM process and through it gain moreexpertise, still has to be completed. Component 2 call for the setting up of the National Support Program, a requisite of the institutionalization process within the DENR. The NSP was legally established as it was adopted by both the past and present administrators. At present, it is starting to set the ground for operations, although the challenge, of how to operationalize it with its present resources, mostly human resource and systems developed by the Local EPM, remains to be addressed.
28 Governance for Philippine Agenda 21	CIDA under the Phil-Canada Development Fund	Philippine Council for Sustainable Development (PCSD) and NEDA (Executing Agencies) LGUs, regional bodies,	The project aims to build the capacity of major stakeholders in operationalizing sustainable development and to develop and institutionalize mechanisms to mainstream sustainable development and Philippine Agenda (PA) 21 into the various decision-making	1999-2002	20.56 (Forex Cdn$1.03 m)	Grant	Nationwide	Provided as grant from NG to LGU.	The project concentrated in conducting trainings oncomprehensive land use planning (CLUP),sustainable and integrated area development(SIAD), project development, and socialmarketing. At this stage, the project

Program/Project Title	Funding Institution	Implementing Agency	Description	Duration	Loan/Grant Amount (Million Pesos)	Terms and Conditions of Funding Institution	Location	Cost-Sharing Arrangements	Status/Remarks
		and communities (implementing agencies)	processes within government and other sectors of society, at all levels of governance. Localization, as a sub-program, is envisioned to formalize the set-up of institutional mechanisms for sustainable development at the local level. The components are: a. Formulation of the Local Agenda 21 - to establish mechanisms and insitutionalize techniques in local planning and local capability building; b. Creation and establishment of local councils for sustainable development and similar structures; c. Mainstreaming PA 21 into local development plans and policies; and, d. PCSD Secretariat support to the National Project Management Unit.						has giventhe Local Councils for Sustainable Dev't. atpilot sites the needed tools for projectimplementation and policy formulation basedon sustainable development (SD) principlesof PA 21. Newly-elected local officials wereoriented in SD. Continuing are activitiesrelated Local Agenda 21 (LA 21) formulation:organizational meetings, existing plan reviewsand consultative stakeholder meetings. ButLA 21 completion would likely happen by1st quarter 2002 . Government sectorconsultation was conducted, and will culminate in island-cluster consultation workshops involving business, civil society and government, outputs of which are recommendations to the President due on1st quarter of next year.
29 Coastal and Marine Biodiversity Component - Mindanao Rural Development Project	Global Environmental Fund	DENR	The project is a component of the Mindanao Rural Development Project of the Department of Agriculture. The GEF will finance the incremental costs of promoting coastal and marine biodiversity conservation and sustainable use in the coastal waters of Mindanao. It aims to remove barriers to mainstreaming marine and	2001-2003	TPC $1.25 m	Grant	Mindanao Island	Provided as grant from NG to LGUs.	
			coastal biodiversity conservation in coastal development by (a) establishing community-based management of marine sanctuaries; (b) strengthening local capacity to sound ecosystem management and decision-making, including monitoring and evaluation for sustainable long-term marine ecosystem management; and (d) developing policy and action plans for marine biodiversity conservation and mainstreaming it into coastal development plans. The components are: a. Resource assessment survey of selected conservation sites; b. Participatory planning and management process for identification and development of protected areas; c. Strenthening of local marine resources surveillance by coastal communities; d. Monitoring and evaluation program; e. Assistance to the development of alternative income geneating activities; and, f. Training of DENR/BFAR officers, LGU/NGO/PO staff.						
30 Leyte Bufferzone Forest Management and Reforestation by Smallholder Communities Project	German Government thru GTZ	DENR, Provincial Government of Leyte and Provincial Government of Southern Leyte	The project aims to assist the smallholder families living in selected upland areas of Leyte island to earn sufficient income while sustainably managing their natural resources. It also aims to strengthen local government and non-government initiatives by supporting participatory planning and maintenance of productivity of natural resources with short-term needs of smallholder households. The key result areas are: a. Economically viable and agroforestry management systems have been elaborated and tested on pilot basis. b. Potentials of additional or alternative income-generating activities have been screened and tested. c. Upland farming families' access to markets, credit and other relevant agricultural and non-agricultural services has improved. d. Sustainable systems for rehabilitation of forests. e. Upland farmers, farmers' organizations, LGUs and other relevant institutions have been upgraded such that they are able to apply the principles of sustainable land use.	2001-2003 (First Phase)	DM 3.5 million	Grant	Pilot sites within the provinces of Leyte and Southern Leyte have yet to be identified.	No pre-determined cost-sharing arrangements. LGUs are expected to provide in-kind contributions for operating and administrative costs. German contribution will be in the form of short-term experts, supply of equipment and expendable materials, training and upgrading of extension officers and target groups, production of teaching materials and publications, local subsidies for self-help measures and a portion of operating and administrative costs.	
31 Tacloban Urban Development and Environmental Management Project	German Government thru GTZ	Municipality of Tacloban	The project aims to ensure that local environmental management in Tacloban is planned and implemented in a participatory manner, taking due account of the economic and social needs of the urban population. The key result areas are: a. Improved capabilities of the LGU Tacloban City with respect to local self-government and the steering of sustainable urban development. b. Activity areas have been identified in the field of environmental management and small-scale projects have	2001-2003 (First phase)	DM 4 million	Grant	Tacloban City	No pre-determined cost-sharing arrangements. LGUs are expected to provide in-kind contributions for operating and administrative costs.	

Program/Project Title	Funding Institution	Implementing Agency	Description	Duration	Loan/Grant Amount (Million Pesos)	Terms and Conditions of Funding Institution	Location	Cost-Sharing Arrangements	Status/Remarks
			been implemented in the upland, urban and coastal zones of Tacloban. c. The prerequisites for improving solid and liquid waste management and the drainage systems have been clarified and initial measures have been launched.						
32 Integrated Community-based Coastal Zone Management-Silago Bay	German Government thru GTZ	DENR Region VIII Provincial Government of Southern Leyte	The project envisions that households in the project area rehabilitate and use their coastal resources in a sustainable manner. The key result areas are: a. The foundations for the sustainable utilization of community marine and freshwater resources are secured. b. The potentials for applying sustainable land-use systems have been surveyed and concepts for increasing production based on upland and lowland resources have been developed and are being tested. c. Community self-organization and the capacity of municipalities and barangays to provide services are strengthened. d. The performance capability of the responsible specialized authorities and the provincial government in the field of coastal zone management is strengthened. e. Projects to promote new and additional income-generating opportunities have been identified and are being tested on a pilot basis.	2001-2003 (First phase)	DM 3.5 million	Grant	Silago, Southern Leyte	No pre-determined cost-sharing arrangements. LGUs are expected to provide in-kind contributions for operating and administrative costs.	
D. *Governance*									
33 Local Development Assistance Program (LDAP)	USAID	DOF-BLGF	The program aims to establish a foundation for sustained economic and social development through policy reforms that will lead to LGU autonomy. It concentrates on local governments responsible for smaller towns and rural areas. The specific components or modes of implementation are: a. Policy-based cash transfer to the Philippine Government amounting to $45 m (budget support); b. Studies/contracts associated with rural development for monitoring, policy studies and technical services; and c. Cooperative agreement with PBSP for managing sub-grants to support decentralization.	1990-1993	US$50 m (USAID) US$16.7 m (GOP)	Grant	Nationwide	RPTA component provided as grant from NG to LGUs.	
34 Local Government Support Program (LGSP) Phase I	CIDA	NEDA (Executing Agency) LGUs (Implementing agencies)	The LGSP is designed to strengthen the capacity of national, regional and local government authorities to develop and implement policies and programs supportive of the Philippine government decentralization. The project focuses on capability-building initiatives such as research, training, policy advocacy, workshops, conferences, technical and managerial expertise, community organization and mobilization, feasibility studies, development education, etc. Priority will be given to actively involving, community-level beneficiaries as participants in their own development.	1991-1998	(US$18.83 million)	Grant	Provinces Identified: Antique Negros Occidental Zamboanga del Sur Zamboanga del Norte Basilan Lanao del Norte Cotabato Agusan del Norte Agusan del Sur Surigao del Norte Surigao del Sur Lanao del Sur Maguindanao Tawi-Tawi	Provided as grant from NG to LGUs.	Completed; total of 315 LGUs were beneficiaries from 28 provinces, 24 cities and 263 municipalities.
35 Philippine Rural Institutional Strengthening Program (PRISP)	EU	Department of Agriculture (DA-lead agency), LGUs and other line agencies such as DA, DAR, DENR, DAP, LGA and NEDA	The project gives special focus on introducing and strengthening participatory planning at the municipal and barangay levels. Through the application of participatory planning, socio-economic development activities will be enhanced because of the active participation and contributions of the local people. Thus, the development activities are expected to respond more closely to the real needs of the local communities because of their involvement in the setting of priorities.	1993-1999	228.00	Grant	Provinces Identified: Nueva Ecija Isabela Negros Oriental Siquijor Davao Oriental Surigao del Sur	Provided as grant from NG to LGU.	Completed in March 1999. PRISP has conducted the Municipal Planning training program in 41 municipalities in 5 provinces, producing 10 draft environmental master plans. Participatory Planning (PP) has been implemented in 6 provinces (covering 192 barangays) with a total of 105 formulated Barangay Development Plans (BDPs). In total, 31 TA interventions (Project Identification, Preparation and Appraisal or PIPA), and Project Design) have been provided, resulting in LGU-prepared project proposals. In program and products marketing, PRISP made a presentation on its MP and PP approaches during the "National Trainors' Training for the Re-Tooling Program" of DILG field officers and staff, which could lead to the possible integration of the

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									approaches in the DILG's training programs. More that 70% of the projects identified by the LGUs through the PP process were approved for funding and are now operational. In addition, as a result of the training programs in PIPA, Project Design and other technical assistance interventions, 77 project proposals were designed and packaged.
36 Governance and Local Democracy (GOLD) Project	USAID	NEDA (Executing Agency) LGUs (Implementing Agencies)	The project is designed to catalyze and reinforce the democratic decentralization process through: (a) strengthening participatory mechanisms in local governance; (b) supporting local government action areas in resource mobilization and management, environmental planning and management, investment promotions and prioritization; (c) supporting Leagues of LGUs and NGO networks; and, (d) institutionalizing a communication and feedback system. The project will be working on a "demand-driven" basis where local communities themselves define the areas where assistance is most needed.	1994-2001	1021.80 (Forex $27.50 m) (Local P306.80 m based on attributions derived from development expenditures (in IRAs) of LGUs and LGU contributions to the Leagues.	Grant	Provinces/Cities Identified: Bulacan Santiago City (Isabela) Nueva Vizcaya Palawan Naga City Bohol Capiz Negros Oriental Lanao del Norte Cotabato General Santos Sarangani	Provided as grant from NG to LGU.	GOLD's biggest contributions are the integration of local governance principles in NGO and PO area development programs, emergence of a new development culture, effective local governance and people participation, electronic governance in Bulacan, democratization and decentralization in Nueva Vizcaya, technology transfer, sharing of non-copyrighted documents, simplified management terminology, empowered local training institutions, validated bottom-up governance approach, and improved confidence in LGU participation.
37 Integrated Rural Acceptability Planning (IRAP) Phase II	Dutch Government	DILG, Local Government Academy (LGA), ILO	The project will develop the planning capacity of selected LGUs using new, simple, and easily applied tools to identify and prioritize projects at	1995-1997	(US$650,796)	Grant	Regions Identified: VI, X and XI	Provided as grant from NG to LGU.	
			local levels. The IRAP procedure is anchored on an assessment of the rural household's access to basic goods and services in identifying interventions and projects to improve living conditions in rural communities. Integration of the IRAP procedure into the planning practices of LGUs will be done by a strategy based on Concentration, Consolidation and Institutionalization. The outputs required to achieve the objectives are: (a) IRAP procedure applied in 9 provinces in Regions VI, X, XI and XIII and consolidated in the other 11 provinces; (b) said LGUs develop and selectively implement effective programs and projects based on IRAP; (c) capacity installed in the LGA to provide technical assistance and training to LGUs on IRAP; (d) awareness of both policy and decision-makers on the usefulness and need for IRAP-based planning; (e) trainors in regional universities capable of training LGUs in the application of IRAP; and, (f) operational IRAP dabatase established in LGA.				Nine provinces (Phase 2) 19 provinces since Phase 1		
38 Technical Assistance for LGUs through the Project Development Assistance Center (PDAC)	Spain (AECI)	National Economic and Development Authority (NEDA)	The project provides direct assistance in the upgrading of LGU internal capability in project formulation and enhancing the capabilities of PDAC in providing assistance to LGUs in terms of project formulation.	1997-1998	8.21	Grant	Nationwide	Provided as grant from NG to LGU.	
39 Strengthening the Decentralized Capability-Building Efforts Towards Sustained Local Development	UNDP	Development Academy of the Philippines (DAP)	The project will support the government's strategy to decentralize capability-building program for LGUs through: (a) strengthening the institutional capabilities of the Institute of Local Government Administration in performing their role as technical resource and training insitutions, to be more responsive to the development needs of LGUs; (b) developing an HRD Program for selected provinces, which will serve as basis in establishing sets of interventions to ensure sustainability and proper application of capability-building programs at the local level; and, (c) strengthening resource institutions such as the Local Government Academy and the Development Academy of the Philippines.	1997-2000	(Forex $852,000) (Local P5.35 m)	Grant	Provinces Identified: Ilocos Sur (Vigan) Northern Samar (Catarman) South Cotabato (Koronadal) Lanao del Norte (Tibanga) Maguindanao	Provided as grant from NG to LGU.	Completed in end 1999.
40 Philippine-Australia Governance Facility (PAGF)	AusAID	Various implementing agencies PAGF caters to government and semi-government	The goal of the facility is to improve the efficiency and effectiveness of Philippine government policies, programs and projects in lowering poverty and improving equity through assistance to government and private sector organizations within the Australia-	1999-2004	A$25.0 m	Grant	Nationwide	All proposals require counterpart funding from the proponents. However, no percentage requirement was	Results of an internal review of PAGF, discussed in a Facility Executive Committee meeting on 8 June 2001, revealed the ff needs: 1. Development of a chart to keep track of developments for each activity/subproject.

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		agencies, LGUs (particularly in Mindanao), NGOs and POs (with national/ regional mandate in So. Philippines), private development organization (partners with government and local communities), anti-corruption and pro-democracy institutions, judicial/legal and professional organizations, Leagues of LGUs.	Philippines Country Strategy guidelines. It is designed to provide timely, responsive and appropriate support to governance initiatives at the national, regional, and local levels in the Philippines using appropriate Australian regional expertise. The value of any single activity to be funded under the PAGF will not exceed A$500,000 (approx. P11 million) and one year in duration. The specific components are: a. Development of Economic and Fiscal Problems; b. Improved Expenditure and Revenue systems; c. Development of pro-poor regulatory framework; d. Development and implementation of sectoral policies affecting livelihood of poor people in four key areas - greater access to health and education, increasing incomes, improving the environment, monitoring, information and statistics, program and project evaluation; e. Civil service reform and reduction in corruption; f. Support to devolution; g. Assistance to civil society and business organizations; and, h. Participation and democracy.					provided in the PAGF brochure.	2. Focus on implementing approved sub-projects and reduce the backlog. 3. Additional staff as possible to work on activity design and implementation, the bulk of Facility workload. 4. Broadened consultants pool, individual pool members and company listings (with capability statements). 5. Faster tendering and contracting methods (I.e. exchange of letters with contractors) with progressive engagement as the context. 6. Consultation with Contract Service Group of AusAID on possible use of period contracts and direct contracting to speed up tendering process. 7. Monitoring framework aligned with AusGuide format. 8. Revisiting of the Participatory Design concept, particularly demands made upon proponents.
41 Philippines-Australia Local Sustainability (PALS) Program	AusAID	Provincial Government of Misamis Occidental (as Executing Authority) Implementing Agencies: municipal LGUs, barangays peoples' organizations	The program expects to strengthen the participatory planning (PP) process and local management of resources (physical, human and financial) for the promotion of sustainable community livelihood. It will support the participatory development planning process and management of priority activities by (a) providing assistance to strengthen LGUs and	1999-2004	356.20 (Forex A$11.99 m) (Local P42.48 m)	Grant	Misamis Occidental	GOP/LGU Contribution: For component 1 - A$195,050 For component 2 - A$1,468,050 For component 3 - A$36,000	Household survey to generate needed information on barangay profiles and population of indigenous peoples completed; enhanced were 33 completed barangay development plans. Municipal technical working committees operational. There is ongoing work on new, more detailed MOAs
			community organizations, and (b) improve delivery through mechanisms that would foster collaborative partnership among all stakeholders. The components are: a. Community and LGU Resource Planning and Management (P56.5 m) - capacity developed in 6 municipal LGUs and 153 barangays therein; b. Program Development (P240 m) - sustainable projects improving livelihoods at barangays, municipal LGUs and provincial LGUs levels; c. Program management and monitoring (P32 m) - activities implemented efficiently, monitoring and evaluation accomplished and reports submitted.					Total : A$1,699,100 AusAID Contribution: For component 1 - A$2,160,500 For component 2 - A$8,547,500 For component 3 - A$1,291,000 Total : A$11,999,000 Grand Total: A$13,698,000 GOP contribution : 12% of grand total	with pilot sites, towards further reinforcement of commitment to Program-related taks. Still ongoing are 19 income-generating sub-projects (I.e. corn-farming, fish cages, and carabao dispersal). More research and technical guidance needed to address implementation problems.
42 Local Government Support Project II	CIDA	Local Government Academy (LGA) of the Department of Interior and Local Government	The project is designed to strengthen the capacity of national, regional and local government authorities to develop and implement policies and programs in support of decentralization. The focus of the project is on capacity-building through, among other things, research, training, policy advocacy, workshops, conferences, technical and managerial expertise, community organization and mobilization, feasibility studies, development education, etc. Priority will be given to actively-involving, community-level beneficiaries as participants in their own development. The components are: a. Organizational Development and Institution Building; and, b. Integrated Area Development for Basic Service Delivery.	1999-2005	749.75 (Cdn$30 m-total)	Grant	Aklan, Antique, Capiz, Guimaras, Iloilo, Negros Occidental (Region VI) Zamboanga del Norte, Zamboanga del Sur, Basialn (Region IX) Misamis Oriental, Misamis Occidental, Bukidnon (Region X) Davao del Sur, South Cotabato, Saranggani (Region XI) Kidapawan, Marawi City, Lanao del Norte, North Cotabato, Iligan City, Cotabato City (Region XII) Agusan del Norte, Butuan, Surigao del Norte, Surigao City, Agusan del Sur (Region XIII) Lanao del Sur, Maguindanao Sulu, Tawi-tawi (ARMM)	Provided as grant from NG to LGU.	LGSP II has lagged in its implementation of sub-projects: less than half (9 our of 11 National PMO subprojects are operational. Currently the project works with a total of 213 LGUs consisting of 30 provinces, 10 cities and 173 municipalities.
43 Training Services Enhancement Project for Rural Life Improvement	Japanese Gov't through JICA	DA-Agricultural Training Institute	The specific technical assistance components are: a. Data information/survey system; b. Project management and organization;	(5 years)	178.2 (Grant P156.6 m) (GOP P21.6 m)	Grant	Bohol - Municipalities of Corella, Loboc, Duero, and Clarin.	Technical assistance provided by ATI. Funding and fund sourcing	Institutionalization of the project in the regular program of ATI and its network of training centers is now

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			c. Training; d. Infrastructure; and e. Equipment and investment outlay.				Gosoon, Butuan Guinobatan, Albay Patnongon, Antique Dupax del Sur, Nueva Vizcaya Sta. Barbara, Pangasinan Eastern Samar - Municipalities of Maybocog and Maydolong	by the LGUs and its clients. Equipment and investment outlay by JICA and ATI.	ongoing.
E. ***Rural and Urban Development***									
44 Decentralized Shelter and Urban Development (DSUD)	USAID	DILG, DOF, DPWH, LMB, HUDCC, NHA, NHMFC	The project aims to foster a greater role for elected city governments, the private sector and NGOs in the development of shelter-related infrastructure in chartered cities in order to increase the access of low-income urban Filipinos to shelter and services over an extended period of time. It aims to (a) develop a sustainable system of city government finance, (b) reduce urban and environmental infrastructure constraints on economic development; and (c) improve access to urban shelter delivery system. The specific components or modes of implementation are: a. Housing Guaranty Program (US$50 m in loan); and, b. Technical assistance and training (US$4 m in grants) for policy analysis, systems and development studies, support to key public, private and NGO groups advancing the policy dialogue and related training and conferences.	1990-1994		Grant	Cabanatuan City Iloilo City Bacolod City Tangub City Batangas City Dagupan City Lipa City Butuan City Cebu City Naga City	Provided as grant from NG to IGU.	Completed.
45 Cavite-Laguna Urban Development and Environmental Management Project Phases I and II	WB	NEDA (executing), LGUs	The project aims to assist in planning and implementation of critical investments for urban and environmental problems in fast growing areas south of Manila and identify projects to support strategies designed to address needs of Cavite and Laguna. The specific activities are: a. Preparation of an integrated urban and environmental management plan using cluster approach to land management for 13 cities/municipalities referred to as Metro	1996-1998	$ 970,000	Grant	Cavite Cluster: Carmona, GMA, Imus, Dasmarinas, Silang, Gen. Trias, Trece Martirez Laguna Cluster: San Pedro, Binan, Sta. Rosa, Cabuyao, Calamba and Los Banos.	Cost-sharing of LGUs in the preparation of the Comprehensive Land Use Development Plans: 1. Gen. Trias, Cavite; 2. Binan, Laguna; 3. Sta. Rosa, Laguna; 4. Cabuyao, Laguna; 5. Calamba, Laguna.	Completed.
			CALA. The output is the "Cluster Land Management and Development Strategy Report" which aims to promote inter-local planning for urban development and cross jurisdictional approach to addressing common problems as traffic management, waste management and adequate housing. b. Preparation of Comprehensive Land Use and Development (CLUDP) and its Implementation Framework for Gen. Trias (Cavite), Binan, Sta. Rosa and Calamba (Laguna).					Each LGU provided P634,000 for counterpart which is 33% of total cost; WB provided the remaining 67%.	
46 Philippine Regional Municipal Development Project (PRMDP)	AusAID (grant component)	DILG (Executing Agency) LGUs (Implementing agencies)	The project has two major components: (1) provision of infrastructure and municipal services; and (2) capability building program. The infrastructure subprojects are demand- based. The TA component includes (a) land- related information system (computerized land information system, computerized system for recording industrial and commercial establishment,computerized collection system); (b) engineering and solid waste management (computerized asset register, manuals for infrastructure and SWMS systems, training and support in their application, effective testing system for soil, aggregate, bitumen, water quality and drainage design, master plans for drainage, solid waste management and water supply; (c) planning and development (improved systems for comprehensive plans, including improved development control system, program for NGO and private sector service delivery, public information programs; and (d) human resources development (supervision system for officer skills, competence and management training, supervision system for service quality and coverage).	1996-2001	Aus$19.12 m) (Forex A$17.27 m) (Local A$4.53 m)	Grant	Lucena City Puerto Princesa (Palawan) Bacolod (Negros Oriental) Tagbilaran (Bohol) Iligan City (Lanao del Norte) Cagayan de Oro City (Misamis Oriental) General Santos (Cotabato)	Provided as grant from NG to LGU.	Bacolod will implement trafficmanagement under the ADB package but will not avail of the loan.It will be a beneficiary of the AusAID package. Cagayan de Oro will benefit only from the AusAID package.
47 Advisory Services for Rural Water Supply and Sanitation in Selected Regions	GTZ	DILG	The project supports rural self-help groups and the population of rural areas to improve the quality and quantity of water supply and hygienic conditions. Insitutional strengthening, capability building and securing the project's sustainability as well as coordination and integration of activities of the various	1999-2001	DM 2.35 m	Grant	Bantayan Island - Bantayan, Santa Fe and Madridejos (Cebu) Asipulo, Hungduan, Tinoc, Lagawe and Mayoyao	No pre-determined cost-sharing arrangements. LGUs are expected to provide in-kind contributions for operating and administrative costs.	Workshops have been conductedin all sites and training activitiesare now ongoing. In BantayanIsland, work is in progress in the formation of the waterworks office.The Provincial Government ofBantayan has committed to provide seed money for the

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			sectors and groups will be undertaken. National suppport to LGUs nationwide regarding the establishment of IWRM shall be provided.				(Ifugao) San Mariano (Isabela)		initialcost of setting and making theOffice operational. The program may run until 2008.
48 Cebu Socio-Economic Empowerment and Development (SEED) Project	Japan International Cooperation Agency (JICA)	Cebu Provincial Government	The primary objectives is the development of an efficient Local Development System within the provincial government and local government units through the implementation of practical activities relating to basic human needs (BHN) and livelihood generation in cooperation with the concerned communities. The expected outputs of the project include (a) strengthened organizational capability of the provincial government and the local government units in development administration and (b) the development of applicable models of sustainable and self-reliable participatory local development. The specific components are: a. Enhancement of administrative capability - function and role survey on administrative institutions concerned after decentralization; establishment of local database system of respective LGUs; training for provincial and LGU staffs; management of BHN pilot activities; monitoring and evaluation for BHN activities; and strengthening institutional mechanism of research and study system in support of said activities; and, b. Development of participatory local development models - situation analysis and needs survey in pilot areas; implementation of pilot BHN activities; implementation of pilot livelihood generation activities; capability building of peoples organizations in management of said activities and enhancement of partnership among LGUs, POs, and NGOs.	1999-2004	242.00 (Forex P220 m) (Local P22.0 m)	Grant	Cebu Province	Provided as grant from NG to LG.	Ongoing activities include the constructionof a waterworks system for 1municipality, and the expansion of 2 others.Improvements were made on farm-to-marketroads, and water resource development completed. Additional manual weavingequipment provided for the Municipal TrainingCenter, which has ongoing training activities.Previously completed were the wastewatertreatment facility (operational 24 hrs a day),public market drainage (for flood alleviation),and a waterworks system for 1 municipality.Construction of an integrated waste management/organic fertilizer facility was moved fornext year. Livelihood component - the ongoing province wide cattle aritificial insemination program of National Government in cooperation with the project has already yielded confirmed cattle pregnancies. The now organized farmers are already utilizing in pilot test mode the machinery for Maguey fiber production. Paper recyclingin selected schools operational. Providedwere additional equipment for charcoalbriquette production, as well as training andtools for livestock health care and a pump-boat and materials for ongoing seaweedsproduction. Building construction for hand-loom weaving project completed. Farmerswere trained in enhanced corn farming andintegrated pest management.
									Capability Building component - finalized NGO implemented study on local development partnership and decentralization has determined areas and mechanisms of stake-holder coordination/collaboration in implementation of development projects.

Sources: Various reports and documents from DOF-MDFO, NEDA, executing/implementing agencies, and donor country programs.

Selected Examples of International Experience with Specialized Municipal Funds

Institution:	Ownership and Management	Funding and Operation:	Security for Debt Issued by Fund	Security provided by Local Governments to Fund
New Hampshire Municipal Bond Bank *One of about 17 bond banks established by states in the US.*	Non-profit, independent unit of State Government. Administered by a 5 member Board of Directors including the State Treasurer. One director shall be a designee of the New Hampshire Municipal Association.	NHMB periodically issues its own bonds (typically twice per year) to cover borrowing requests made by local government institutions. Requests are approved and pooled during the period between bond issues. Tenor and interest rate of loans made to local governments are matched with those obtained in its own bond floatation to avoid interest rate risks.	Self–supporting reserve fund equal to maximum annual debt service. No State government guarantee, but NHMB can request an advance of State funds to maintain legally required level of debt service reserve.	Intercept of State payments to municipality in case of non-payment. Full credit of local government borrowers in case of general obligation bonds or revenues from income earning public utilities in case of revenue bonds.
Municipal Finance Authority of British Columbia, Canada (MFA) *One of six Municipal Finance Corporations established by Canadian provinces.*	Provincial Government corporation administered by a Board of Directors. The Directors are elected from Regional Districts of the Province based on the population of the Region. No provincial level official sits on the board.	MFA issues its own bonds about twice yearly to cover pooled borrowing requests by Regional Districts and local government institutions during the period. The MFA faces limited interest rate exposure as the Authority's initial borrowing does not always correspond in tenor and interest rate to related loans that it makes to regional districts.	No Provincial Government Guarantee. (The Municipal Funds of other Canadian Provinces do benefit from a Provincial guarantee). Borrowers contribute to a Debt Reserve Fund and a sinking fund as well as a special liquidity fund. These funds are supported by payments from borrowers over and above interest and principle payments. The MFA was granted power to levy a special tax on property in the Province in case debt-reserve fund is inadequate.	Unconditional pledge of borrowers to meet obligations. The member municipalities are jointly and severally obligated to the regional districts for the debt issued on their behalf.

Kommuninvest of Sweden *One of several municipal lending institutions in Nordic countries including Norway, Denmark, and Finland that follow communal approaches.*	Limited liability, non-profit company owned by a cooperative society of local and county councils. At present 109 municipalities and councils are members of the society. Administered by Board of Directors. Membership is voluntary, but members subject to scrutiny. Members must buy capital to join.	Frequent domestic and international bond floatation to cover borrowing requests by local government institutions. Similar to "credit union" style of operation. Terms for borrowing and lending are matched exactly to avoid interest rate and currency risks. When different currencies are borrowed, the policy is to use currency swaps to reduce currency and interest rate risks.	Full guarantee by Swedish Government.	The society's members sign an unlimited joint and several guarantee to cover credit liabilities of Kommuninvest. In case of a call on the guarantee, demands will be apportioned based on the individual municipality's liability to Kommuninvest.
Japan Finance Corporation for Municipal Enterprises (JFM)	Fully owned by Government of Japan.	JFM issues publicly offered bonds, both domestic and foreign. JFM is exposed to interest rate risk, as the average maturity of its bonds is 10 years while it makes loans of up to 28 years.	Unconditional guarantee by GOJ.	Revenues from enterprises. Pledge from responsible municipality.
Tamil Nadu, India	Autonomous Financial Intermediary. Tamil Nadu State ownership of equity restricted to maximum of 49%. Private equity 51%. Managed outside government by a specially formed private fund management company.	Domestic bond floatation. Loan from World Bank Private sector municipal service providers are eligible to borrow in addition to units of government. Grants to urban local bodies for feasibility studies, detailed designs and training are available from a separate grant fund.	The domestic bonds issued by fund are not guaranteed either by the state on national governments. World Bank loans are guaranteed by national government.	Full faith and credit of borrowing government. Municipalities must establish an escrow account in which property tax revenues are deposited. Fund has first claim on account. Revenue flows from revenue earning projects.

Findeter, Columbia	Autonomous, quasi-public financial organization. Shares held by Ministry of Finance (86%) and regional governments (14%).	Operates as a bank by channeling its loans through approved primary lenders, mainly commercial banks. Findeter does not lend directly to Local governments. Findeter rediscounts up to 85% of the loan amount from the primary lender. Primary lender provides 15% of loan amount from own resources and primary lender bears all credit risk. Findeter lends with tenor of 8 to12 years, which is longer than normal commercial bank tenor of 3 to 5 years. The facility allows primary banks to lengthen the term of loans without incurring a maturity mismatch.	The Government of Columbia guarantees loans from World Bank and Inter American Development Bank.	Primary lenders are responsible for repaying Findeter loan. Primary lenders receive pledge of revenue transfers (voluntary intercept) due from central government; also revenue from tariffs and fees from revenue generating projects. Primary lenders are often depository banks of local governments, which increases security.
Parana, Brazil	The State of Parana owns the resources of the "Fund" for Urban Development. The Fund is managed under a contract with a specially set up non-profit corporation (known as Paranacidade), which has private sector legal status. In some cases Paranacidade authorizes local government associations to screen projects from their region of the state to promote local responsibility.	The Fund is financed by loans from the World Bank and Inter American Development Bank. Parana State agreed to repay international loans made prior to 1996 when the management contract was signed. This allowed the Fund to benefit from re-flows. All debt incurred by the Fund after 1996 is repaid by the Fund. This exposes the Fund to exchange rate risks.	Loans from World Bank and Inter American Development Bank guaranteed by the Government of Brazil.	The Parana fund requires borrowers to pledge transfers form the State government (a voluntary intercept). Municipal loans carry the full pledge of the borrowing municipality.