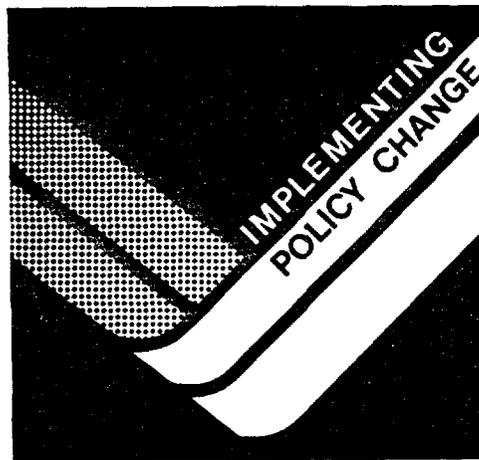


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IMPLEMENTING POLICY CHANGE IN THE PHILIPPINES: The Support for Development II Program (Final Report)

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**IMPLEMENTING POLICY CHANGE IN THE PHILIPPINES:
THE SUPPORT FOR DEVELOPMENT II PROGRAM
REVISED REPORT OF ACTIVITIES
FINAL VERSION**

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C

LIST OF ACRONYMS

| | |
|---------|---|
| BIR | Bureau of Internal Revenue |
| BOI | Board of Investments |
| BOC | Bureau of Customs |
| BSP | Bureau of Statistics & Planning |
| Center | One Stop Shop on the duty drawback and the VAT credit |
| DOF | Department of Finance |
| DTI-BOI | Department of Trade & Industry - Board of Investments |
| EO | Executive Order |
| GOP | Government of the Philippines |
| IRS | Internal Revenue Service |
| NEDA | National Economic & Development Authority |
| NIRC | National Internal Revenue Code |
| NPC | National Power Company |
| PIDS | Philippine Institute for Development Studies |
| RAMO | Revenue Administration Memorandum Order |
| RR | Revenue Regulation |
| SDPII | Support for Development Project II |
| TCC | Tax Credit Certificates |
| TCCP | Tariff and Customs Code of the Philippines |
| USAID | United States Agency for International Development |

1. BACKGROUND

1.1 Introduction

This final report of the SDP II support activities funded under the IPC project proposes to focus on major accomplishments during the implementation period organized according to the scope of work components:

- Streamline Duty Drawback and VAT tax credit
- Management Information System/Monitoring and Evaluation
- Strengthen VAT Administration

Each section also describes further steps required to sustain the functions described. The emphasis in this report is on what was done and what can still be done to achieve objectives rather than an overly historical description of the progress in assisting the organizations involved in SDP II implementation and monitoring. It is the judgement of the team that this more straightforward approach might be welcomed by GOP and USAID decision-makers reviewing our work. Given that a large number of written products (32 or more) have been produced, it is possible to get a rather detailed picture of our work by reviewing them (See Annex 2, Technical Reports Produced by SDP II IPC).

Our report naturally enough offers some overall conclusions from the work and ends with a few recommendations for consideration.

The team would like to thank Dr. John Chang, Program Economist, USAID/Manila for his consistent leadership and advice in completing this work and the members of his staff who assisted our efforts. Dr. Maria Cecilia Soriano, Undersecretary, Department of Finance when the activities began provided extremely valuable guidance in the first year of the work. The project would also like to acknowledge the contributions made by Secretary Roberto de Ocampo, Department of Finance; Undersecretary Romeo Bernardo, Department of Finance; Undersecretary Juanita Amatong, Department of Finance; Assistant Secretary Antonio Belicena, Department of Finance; Commissioner Guillermo Parayno, Bureau of Customs; Commissioner Liwayway Vinzons Chato, Bureau of Internal Revenue; Director Ofelia Templo, National Planning and Policy Staff, NEDA; Assistant Director Narcisa Umali, National Planning and Policy Staff, NEDA; Atty. Uldarico Andutan, Administrator, One Stop Shop-Duty Drawback Center; Assistant Director Estelita Aquirre, Bureau of Internal Revenue; Deputy Commissioner Victor Dioferio, Bureau of Internal Revenue; and Undersecretary Tomas Alcantara, Department of Trade and Industry. Without their guidance and insights we would not be able to report the progress documented in this report.

1.2 Work Objectives

The Support for Development Program (SDP) II is a policy-based, Balance of Payments (BOP) support project for the Government of the Philippines (GOP). Specifically, SDP II supports the

implementation of a set of policy reforms aimed at enhancing competitiveness of Philippine exports in the world markets. (See Table 1.)

To achieve this goal, the following objectives have been established: assist the Government of the Philippines (GOP) managers to improve administrative efficiency of the VAT tax credit and duty drawbacks systems; and to assist managers and technical staff to develop and implement a management information system which would track adherence to the SDP II policy matrix, provide the means to anticipate and respond to implementation problems, and help assess impacts on the reforms of exogenous events and the impacts of the reforms on the export sector and the economy as a whole. The emphasis is on assisting the GOP managers to implement selective SDP II policy reforms successfully and to monitor the process under SDP II as a whole. The subsidiary focus is to strengthen the capacity of the GOP agencies to design and implement policy reforms.

To achieve the above objectives, three general tasks have been developed: to streamline the duty drawback system, strengthen the VAT administration, and to design and implement a Management Information System for monitoring and evaluation. Under each task, there are specific purposes and activities for implementation. (See Annex 1 for Complete Scope of Work.)

Streamline Duty Drawback System

This task supports the policy objective of establishing competitive pricing for exports and their inputs, and specifically addresses the issue of access to inputs at world prices. Operation of the duty drawback center involves the participation of a number of GOP agencies including the Department of Trade and Industry - Board of Investments (DTI-BOI) and the Bureau of Customs (BOC).

Activities to be conducted included the following:

- Conduct strategic management exercises to clarify objectives, responsibilities, tasks, and needs; determine whether organizations can accommodate the changes associated with the program; assess whether legislative actions are necessary; and devise a timetable for the implementation of actions for tracking of development and identification of implementation bottlenecks.
- Provide technical collaboration to streamline the duty drawback and VAT tax credit system; assess proposed systems design, computer hardware and software requirements necessary for implementation of the duty drawback system; and design and implement the management information system (MIS) for the duty drawback center.
- Conduct a study tour for the operations management staff to other Asian countries to observe design, operation and management of other duty drawback systems.

Table 1

| Policy Objective/Implementation Action | Performance Indicators | |
|--|---|---|
| | Tranche 2 | Tranche 3 |
| A. Strategy: Competitive pricing of exports and their inputs | | |
| 1. Market-determined foreign exchange rate | | |
| Liberalize foreign exchange | Comprehensive review of foreign exchange rules and regulations completed | Recommendations of the review acted on, including: <ul style="list-style-type: none"> ■ Participation in the foreign exchange market expanded to other banks and nonbank institutions ■ Revised accreditation system for foreign exchange brokers and dealers operating |
| | Retention limits for exporters of their foreign exchange earnings substantially expanded | |
| | Off-floor trading among commercial banks initiated | Review of experience of off-floor trading completed and, if necessary, appropriate adjustments initiated |
| 2. Access to inputs at world prices | | |
| Streamline duty drawback and VAT credit systems | One-stop drawback center operating effectively | Length of processing time for 80 percent of completed applications reduced to 60 days or less for at least three months |
| | Procedures for prompt approval of 40 percent of VAT credit claims implemented | Length of processing time for 80 percent of completed applications reduced to 60 days or less for at least three months |
| B. Strategy: Supportive environment for exports | | |
| 1. Adequate provision of interisland liner shipping services | | |
| Liberalize cargo rate regulations | Action plan adopted to liberalize liner cargo rates | Agricultural commodities reclassified Cargo fork tariffs widened significantly |
| 2. Efficient financial resource mobilization | | |
| Lessen interest rate impact of public debt financing through improved management | Action program adopted for improving the access of small savers to government securities, including possible use of trust units and/or saving bonds | Mechanism or mechanisms for the access of small savers to government securities designed |

- Conduct a study and review to assess the efficiency of the duty drawback center after six months in operation; evaluate the implementing procedures for prompt approval of claims and provide recommendations for improvement; study/design systems to obtain and use customer and staff feedback to determine and implement necessary adjustments to further enhance efficiency; and study the feasibility of decentralizing the new duty drawback systems.

Strengthen VAT Administration

Strengthening the VAT administration will support the policy objective of creating a more conducive environment for exports by enhancing the efficiency of financial resource mobilization. The primary activity is to assess the current VAT administration, enhance its management practices and performance, and to develop and implement management training systems throughout the VAT administration.

Activities to be conducted include the following:

- Conduct a strategic management exercise to clarify objectives, responsibilities, tasks and needs.
- Provide technical collaboration to develop and implement change management programs to strengthen the VAT credit and collection systems.
- Conduct a study and review of the current VAT credit system to generate lessons learned; and design and estimate and econometric model for forecasting revenues.
- Conduct a study tour for VAT division managers to other countries to observe VAT systems and explore key elements of success.

Management Information Systems/Monitoring and Evaluation

This task has been established to assist GOP managers in designing and implementing an information system to measure the achievement of policy matrix objectives and to measure the impact of SDP II's interventions on the Philippines economy.

Activities to be conducted include the following:

- Indicate a process to further refine policy matrix indicators and how and by whom data to measure achievement will be obtained and reported; develop indicators and monitor for influential factors outside of the matrix; and determine what data are important to implementation decisions.
- Assist GOP managers in the conceptual design, development and use of a management information system that can track adherence to the policy matrix; provide the means to anticipate and respond to implementation problems; help to assess impacts on the reforms of exogenous events and the impacts of the reforms on the export sector and the economy as a whole; and develop manuals for MIS.

- Assist the organization of a series of consultancies within the GOP on monitoring and implementing policy actions and technical support under SDP II.

Originally, the proposed project period was from March 16, 1992 to December 31, 1993. However, the period has been extended to May 31, 1994 to allow for the completion of some task component activities.

1.3 Description of Work Methods

Early in the assessment process the IPC team recognized the absolute necessity of performing all analysis, strategic management and training activities with complete emphasis on active collaboration. This approach was maintained consistently despite significant shifts in responsibility and senior posts on the GOP side. Indeed, the changes in the senior management of the institutions directly related to this SDP II activity in particular DOF led to additional training workshops being implemented over the life of the activity. The project (with USAID approval) added workshops and seminars to the number originally planned to give new or re-assigned GOP staff opportunities to sort out how to deal with new institutional realities affecting the performance of the units involved in the work.

As can be seen clearly in the reports of all the training activities, active involvement with participants in planning workshops and seminars was an essential element of the positive responses to these activities. All strategic management workshops included these specific elements to ensure a collaborative process:

- mutually established objectives for workshop outcomes
- heavy emphasis on participatory methods including small group exercises
- utilization of strategic management methods of analysis and tools
- preparation of detailed action plans to ensure continuity and progress in decision-making.

The technical analysis and operations assistance provided to the Duty Drawback Center and VAT relied on collaborative methods as well. In addition to accompanying the reconnaissance-visits to New Zealand and Indonesia, the IPC advisors worked directly with staff at DDB and VAT on a regular basis to ensure that systems suggestions were solidly grounded in GOP realities. Assistance was conducted on the premises of the units being assisted and work schedules were adjusted to those of the GOP colleagues to ensure that their input could be obtained even though they were sometimes heavily involved in operational concerns and adjusting to brownout realities. Because of the complexity of some of the problems being addressed, extra attention was given to producing options for consideration by senior staff rather than formal conclusions. Once the relative value of options were analyzed, final recommendations were made and formalized in reports.

The presence of a Philippine-based team leader on a part-time basis throughout the project has allowed regular contact and coordination. This management attention has been particularly helpful in briefing GOP senior officials interested in the projects and in providing continuity for short-term consultants. A core group of Philippine and U.S. based consultants from IPC were used throughout the project. (See Annex 2 for Summary of Overseas Technical Assistance.)

2. STREAMLINE DUTY DRAWBACK AND VAT TAX CREDIT

This section presents both the major accomplishments to date of the Center for the duty drawback and the VAT credit and highlights issues to which the Center could direct its efforts with a view to making its functions sustainable.

2.1 Major Accomplishments

Review of the Operations of the Center

This section presents a brief overview of the operations of the Center. The majority of the issues discussed in this section are comprehensively covered in our four technical reports on the review of the operations of the Center. (See annex 2 for list of reports)

Legal Framework: The activity of the Center is currently governed by an Executive Order issued by the President of the Republic of the Philippines and a Revenue Administration Memorandum Order issued by the BIR.

The Executive Order (EO) 226 provides for the establishment and the administration of the Center. Its provisions cover the transfer, to the Center, of the processing of the claims for the duty drawback and the VAT Credit from the BIR, the BOC, the BOI and the DOF. In line with the provisions of this EO, the Center started its operations on May 8, 1992.

The EO provided for the establishment of the Center for an initial and temporary duration of one year. However, the status of the Center was made permanent in 1993 with the provision for inclusion of its budget in the national budget.

The BIR Revenue Administration Memorandum Order (RAMO) 2-93 provides for the transfer of processing of the total amount (full processing) of the claim for the VAT credit to the Center. The effective date of the transfer was October 1, 1993. This RAMO excludes the processing of the VAT cash refunds and the processing of the applications of the indirect exporters. The BIR will, in principle, still process these latter types of applications, under RAMO 1-91.

The Center has itself issued a number of internal regulations for the processing of the applications for both the duty drawback and the VAT credit. These regulations are generally concerned with the actual operations of the Center and the manner of the refund of the duty drawback and the VAT credit. There are, for instance, provisions for the processing fees, and fees for the issue and the transfers of the Tax Credit Certificates(TCC).

Organization: The Center was initially structured and organized in line with the function transferred by the EO. It initially centralized the organization of the duty drawback and the VAT refund activities in one location through the physical transfer of staff from each of the related agencies. This represented the four agencies under one location. The Center has since moved towards a integration of its organizational structure. It is now organized based on the regulations governing the refund and by industry into the operations division and other support divisions.

Relations and Coordination: The Center works closely and coordinates its activity with the aforementioned agencies. In general, the bulk of the "refund activity" has already been transferred to the Center. The refunds cover both the exports as well as refunds relating to the fuel sales to the NPC. There remains a limited number of other related refunds which are still processed by the other agencies.

Policies and Procedures: The Center initially followed the same policies and procedures on refunds as they were previously practiced by each of the related agencies. There has been a gradual change in the procedures since the transfer of the processing activities to the Center. The Center is currently in the midst of developing a number of written procedures for processing the applications. It has also introduced a number of revised practices and processes in order to expedite the processing of the applications. The overall effect of all these actions is demonstrated by the fact that the processing period of the applications for the refund has in general been reduced to about a month.

Human Resources: The personnel of Center initially represented the employees of the related agencies who were seconded to the center for an initial period of six months. The Center is currently largely staffed by new hires whose salaries are drawn from revenue collected as the processing fees.

Information Systems: The Center has a management information division which is continuously developing programs for automation of each separate individual activity involved in the processing of the applications. A comprehensive list of the activities which are currently automated is presented in our technical report (Part Three).

Equipment and Other Material Resources: The Center has managed to procure the essential necessary backup support in terms of office equipment and other material resources. A comprehensive review of the computer facilities and equipment was presented in our technical report on the administration of the duty drawback and the VAT credit (Part Three). A portion of this equipment was provided by SDP II funds under the IPC program.

Provision of Technical Assistance Under SDPII

Involvement in the operations of the Center were in line in with the provisions of the scope of our work under Task 1 and part of Task 2 of the SDPII project (see Annex 1).

Strategic Management: IPC consultants Dr. Benjamin Crosby, Norman Bramble, Guia Espiritu and Gabriel Lopez all facilitated the start-up strategic management colloquium on April 4, 1992 for the senior managers of the agencies involved in the activation and operation of a ONE STOP SHOP - INTER-AGENCY TAX CREDIT AND DUTY DRAWBACK CENTER. The agencies represented were: the Department of Finance, the Bureau of Customs, the Bureau of Internal Revenues, and the Board of Investments. The workshop focused on the identification of strategic issues that faced the inter-agency center as it organized and activated itself. A week after, the center's steering committee was formed to set guidelines for the start-up activities of the center.

At about the same time, another consultant, Ms. Lourdes Lopez, was tasked to undertake a stakeholders' analysis of all the perceived parties having interests or were affected by the center's proposed activities. The results of the study were presented to the steering committee in June 1992.

Another strategic planning workshop (the last for the project period) was conducted on March 21, 1994 by IPC consultants Norman Bramble, Guia Espiritu and Gabriel Lopez wherein the main areas for concern were: *Uniformity of Procedures; Standard Rates; Audit and Control; Computerization and Management Information Systems; and Human Resources and Budgeting.* Strategies and action plans were presented to the Chairperson of the Center's Executive Committee, Finance Undersecretary Juanita Amatong, who expressed satisfaction and a strong desire to institutionalize strategic management throughout the Department of Finance.

Training: IPC consultants Norman Bramble, Gabriel Lopez and Guia Espiritu facilitated two workshops for the new staff members of the Duty Drawback Center focusing on teambuilding, values formation, planning of start-up activities, and agreement of operating procedures. These were conducted at the Department of Finance's newly opened *Jaime V. Ongpin Training Center* on April 6-8 and 27-29, 1992.

On October 5-9, 1992 five senior managers of the Center were accompanied by IPC consultant Chip Krakoff on an orientation and study tour in Wellington and Auckland, New Zealand to observe the successful operation of its duty drawback system in its Customs Administration.

On December 12-13, 1992 the Center's staff members held a review workshop in Imus, Cavite to take account of their performance, successes, and problems since the Center started its operations on May 8, 1992. It also served as an opportunity to plan for further improvements in their operations. The workshop facilitators were IPC consultants Norman Bramble, Guia Espiritu and Gabriel Lopez, assisted by Leah Ello, a Coverdale associate trainer.

On June 7-11, 1993 Norman Bramble and Guia Espiritu, assisted by selected Center in-house assistant training coaches, conducted another workshop on teambuilding, values formation, planning and orientation for new staff members of the Center, recruited to replace original staff who had been recalled to their parent organizations, specifically those from the Board of Investments.

Information Systems: Since the start-up of the Center (and until the first quarter of 1993), IPC consultant Gilbert Yu, a computer systems specialist, provided technical assistance to the Center in the design and development of a management information system and computer programs for its use. The final result was a manual for the Center staff.

Study and review: IPC consultant Alice Morton visited the country three times in 1992 (in March, June and October/November) to work with the Center's senior managers and staff in expanding and improving their operating activities. In November, 1992 she accompanied five senior managers in visiting selected exporters' bases outside Metro Manila (i.e. Legazpi City, Southern Luzon; Cebu City, Central Visayas; and Davao City, Southern Mindanao) to find out the impact, if any yet, of the Center's operations on exporters outside Metro Manila. She

consulted with IPC consultant, Atty. Florecita Flores about the need to conduct a survey among members of the Philippine Exporters Confederation (PHILEXPORT) to determine their awareness and use of the Center's services and find out any significant impact on their performance. Said survey was started in collaboration with PHILEXPORT. However, PHILEXPORT was unable to retrieve all of the one hundred fifty questionnaires distributed randomly. Only twenty completed questionnaires were returned. USAID/Manila preferred to drop the activity based on this response.

IPC consultant Nezam Motabar visited the country twice in 1992 (May and November) and three times in 1993 (February, July and November) to assist the professional staff in upgrading their operating systems and procedures. The more detailed, specific technical advice provided is summarized in the sections below.

Performance Report: In 1992 (during its first eight months of operations) the Center issued 1,052 Tax Credit Certificates (TCCs) worth P1.8 Billion to its exporter-claimants. Said amount represented export/inward remittances of P21.13 billion for the same period. Under the *Investment Incentive Mode* 766 TCCs worth P753.71 M were released, comprising 41.92% of total TCCs issued. Of these, the industry groups that benefited most were the *Wearables Industry* (333 TCCs worth P504.08 M), the *Agro-based Industry* (P88.64 M mostly for prawns), and the *Chemicals Industry* (P68.53 M). Under the *Duty Drawback Scheme* 261 TCCs worth P1.01 Billion were released as follows: P867.61 M for *Oil Industry*, P39.49 M for *Agro-based Industry*, and P29.64 for *Service Industry*. Under the *VAT Credit system* 16 TCCs worth P8.51 M were issued, where the *Electronic Industry* received the most, with 6 TCCs worth P4.73 M. For *Government Transactions* P23.12 M were released. It should be noted that the average processing period of tax credit and duty drawback claims was twenty-five (25) working days, ahead of the prescribed thirty (30) days.

In 1993 the Center issued 2,716 TCCs worth P4.1 Billion to exporter-claimants. Under the *Investment Incentive Mode* 2,020 TCCs worth P1.62 Billion were released, wherein the *Wearables Industry* got the most (888 TCCs worth P1.03 Billion). Under the *Duty Drawback Scheme* 609 TCCs worth P2.37 Billion were issued, wherein the *Oil Industry* received the most (120 TCCs worth P1.99 Billion). Under the *VAT Credit Systems* 56 TCCs worth P40.23 M were released, the bulk of which went to the *Mining Industry* (15 TCCs worth P23.4 M). For *Government Transactions* 23 TCCs worth P45.84 M were released. Under the *Order Regalo Scheme* 8 TCCs worth P28.88 M were issued, the majority of which went to *Metals and Engineering* industries. During its second year of operations the average processing period was 32.7 days, above the prescribed 30 days due to the increased volume of applications. However, the bulk of applications still fell within the prescribed period.

In June 1993 a computerized *Automated Receiving and Cashier System* became operational, improving the Center's efficient service. In October 1993 the processing of the entire *VAT Refund* for exporters was transferred to the Center from the Bureau of Internal Revenues by virtue of *Revenue Audit Memorandum Order (RAMO) No. 2-93*. Under the previous set-up, exporters had a choice of availing of the VAT Refund under *RAMO 1-91* or *Ramo 1-93*. Under the former the beneficiary can file 100 % VAT refund claim directly at the Bureau of Internal Revenues, which is mandated to process claims in sixty (60) days. Under the latter, the

beneficiary can file a claim not exceeding 40% at the Center, which is mandated to process claims in thirty (30) days. Afterwards, the application will be forwarded to BIR for processing of the remaining 60% within 60 days. A strict auditing requirement is a common feature of both. The claimants understandably opt to apply directly with the BIR and claim a 100% VAT refund notwithstanding the fact that it takes more than 60 days to process the claims and issue a corresponding TCC. With this transfer, it is expected that claiming tax credit under the VAT Refund Scheme will be streamlined and expedited.

In 1993 the Center received two foreign delegations, from the People's Republic of China and the Democratic Republic of Vietnam. They visited the Center to observe its operations in November.

The Center has fared well since its activation in 1992. Its earlier staffing concerns have been allayed with the provisions of a budget for its personnel and operations by the Department of Finance. It continues to make improvements in its operating systems and procedures through training and acquisition of additional equipment and software. It more than met its targets for released TCCs. Organizationally, it appears more stable with the continued support it receives from the current Secretary of Finance, including its occupation of sizeable work spaces on the ground and third floors of the Finance Building.

Reports prepared under the SDP II technical assistance cover the administrative, technical, operational and other related aspects or issues relative to the Center and its activity for processing the applications for the refund of duties and taxes. We have provided specific technical advice in the following areas:

- Provision of technical advice during and with the implementation of the EO 226 and the RAMO 2-93;
- Provision of technical advice for a processing fee structure (a separate Technical Note was prepared for this purpose);
- Provision of on-going technical assistance with the implementation of audit and verification procedures for processing of the applications for the duty drawback and the VAT credit;
- Provision of technical advice regarding the issue and the transfer of TCCs;
- Assistance in compilation of the requirements for further computerization of the activities of the Center.

The SDPII Project Conditionalities

The conditionalities required for release of Tranche 2 and Tranche 3 of SDPII, supports the two basic policy goals of the program, namely:

STRATEGY A: Competitive pricing for exports and their inputs, and;

STRATEGY B: A supportive policy environment for export development.

The conditionalities address specific GOP activities in four areas. The SDP II agreement also provides for technical support to the GOP in implementing and monitoring policy performance. Our scope of work, as it relates to the technical assistance component under Tasks 1 and 2 (in part), was limited to the area of agreement and the goal as follows:

Access to inputs at world prices, to be partially achieved by means of streamlining duty drawback and the VAT credit.

Tranche 2 requires that the Center operate effectively, and procedures for prompt approval of 40 percent of VAT credit claims be implemented.

Tranche 3 requires that the length of processing time for 80 percent of completed applications for the duty drawback and the VAT credit be reduced to 60 days or less for at least three months period.

The Center has totally met the performance indicators under tranche 2. Under tranche 3, the Center has also met the performance indicators for VAT refund processing completely. (See Table 1. SDP II Matrix)

2.2 Scope For Future Actions to Maintain a Sustainable Position

Analysis of the Operations of the Center

The underlying justification for the establishment of the Center was based on the fact that a speedier processing of the duty-drawback and the VAT credit to the exporters will enable them to compete more effectively at world market prices. The institutions involved in the process: the BOC and the BIR viewed their roles more as revenue collection agencies of the government, rather than providing refunds. As a consequence of this philosophy, their procedures were oriented towards better collection procedures which did not easily translate into a better refund system.

Within an integrated management information system, generally automated, the refund process is merely the mirror image of the payment process. In such a situation, there is usually little need to create a separate set up to deal with the refund. The computerization plan currently underway for the BIR and the BOC will eventually produce databases and management information systems wherein the refund activity can be integrated as part of the payment process. This is generally the experience in other countries where their operations are already automated.

In these conditions, given the fact that the Center has originally been created to fulfill an administrative function, its position as an institution and an inter-agency organization can only be sustained on a long term basis if its functions evolve in a manner which will add value to the efforts of the import-export activity. We propose below a plan of action that the Center should undertake in order to develop the general export environment rather than merely representing a refund processing center.

Based on the above analysis, the Center's function should evolve with the progress in automation and flow of information. This would mean that the Center should possibly orient its activities towards a number of areas, as follows:

- Enhancement of technical standards and operational functions;
- Developing a position as an advisory body, for both the import-export industry, and also on the related issues on economic planning for national purposes;
- Functioning as a regulatory body on streamlining legislation and on micro economic issues.

Each of these is described below.

Enhancement of Technical Standards and Operational Functions

The Center can now move forward from the initial phase of centralizing the refund activity, which has largely been accomplished, towards implementation of a number of other actions. These other actions can be either prioritized or move forward in tandem with each other. These actions should be developed in line with the progress in the automation of the activities both at the Center as well as at the BIR and the BOC. The major actions that should be undertaken are:

1. Development of standards for the calculation of inputs into each specific product, otherwise known as standard rates;
2. Development of audit and verification capabilities for the refunds, compatible with its gradual automation. The Center will, then, be well placed to contribute to the same efforts of other related government institutions which will be automated in the next few years. The Center can, for instance:
 - Develop a gradual change of emphasis on audit approach, by reducing the weight on documentation audit and increasing the emphasis on operational audits;
 - Introduce a change in the methodology for the processing of the claims from the current reactive approach to their processing to a proactive approach; initially starting with the very large clients. This approach would eventually allow more attention to be given to the medium and small exporters as there will be a lesser demand on the total resources of the Center by the large exporters.
3. On-going streamlining of the whole refund process. In this connection:
 - Streamline further the administrative procedures concerning application for a refund through the following steps or actions:

- Introduction of the related changes to the application form;
 - Changes to the processing fee structure in response to streamlining of the operations;
 - The imposition of fines and penalties for violations, in line with streamlining of the operations;
- Streamline further the processing of the claims for a refund through the steps or actions set out below.

The approach that we have already proposed in our technical reports for streamlining the processing of the applications can be pursued further by the Center. The approach is based on the following concepts:

- Integration of the steps for different types of application into one, where the steps are not application based;
 - Consolidation of the different processing procedures currently in use at the Center;
 - Simplification of the practices for processing the applications;
 - Unification of the different processes currently in operation.
- Merging the refund process activity for the VAT credit with the duty drawback;
 - Moving towards deconcentration and an eventual decentralization (regionalization) of the activities of the Center.

In general, it may be argued that the implementation of a number of our proposals would result in the loss of revenue for the government in the short term, and thus it may not be expedient to implement them for economic or political reasons. The majority of such revenues represent economic transfers rather than actual revenues. Though the implementation of the proposals may result in a negative cash flow effect in the short term, it will eventually result in an overall saving in economic resources and will generate additional revenue for both the government and the private sector as the export sector grows.

Developing a Position as an Advisory Body

The advisory function should develop the Center into a body to evaluate the impact of the refunds on a particular product, its related industry and also its sector as it concerns the local economy as well as the world markets. The Center should evaluate the comparative costs, and thus advise the businesses on the import-export policies in conjunction with other government or private bodies involved in the import-export activity. There are a number areas in which the

Center can provide advice and support, for instance serving as a data center for the most cost effective inputs, and accordingly advise the organizations involved in or with the import-export.

Functioning as a Regulatory Body

Functioning as a regulatory body on streamlining legislation and on micro economic issues should initially, at least, involve the Center in streamlining the legislation on refunds.

In general, the government exacts a number of different charges on imports. Irrespective of their designation (i.e. duties and/or taxes), they all represent levies. The manner of application for the refund, the processing procedures (as distinct from the verification procedures which are not normally a function of those charges), and the actual form of and the related procedures for the refund need not be different. This is not currently the case with the refund for the VAT credit and the duty drawback. The multiplicity of the procedures result in an overall economic cost to the country as a whole. Nonetheless, the Center has successfully managed to process the refund within the time period required by the legislation. The achievement is impressive given the constraints within which the Center has been operating.

However, the Center should attempt to influence legislation and/or provide for revised administrative regulations. There are a number of areas in which the Center can pursue and advocate policy changes, namely:

- Propose the required legislation or regulations for a uniform set of procedures for the processing and the issue of the refunds;
- Consolidation of all the regulations, through legislation and administrative regulations.

For instance, The Center should provide for the issue of a common, centralized and unique Tax Credit Certificate (TCC). We have already described in our technical reports the different forms of refund and the difference between a TCC representing a VAT credit versus one representing the duty drawback. The following actions seem called for:

- Issue of the TCCs

The total process involved in the issue of a TCC should be revised. There are certain areas in tax laws and the laws governing tariffs and customs where trade off of the TCC may not be legally or constitutionally possible. The centralization of the issue and utilization of the TCCs will provide against errors and abuse.

- Reuse of the TCCs

There is a need for the conduct of a comprehensive study into the reuse of the TCCs. From a purely business analogy point of view, TCC represents the output or the product for sale by the Center. The manner the TCCs are exchanged, uncashed, traded and refunded will bear directly on the operations of the Center.

It may be in the best interests of the Center to itself regulate a secondary market in the TCCs.

In addition, the information obtained in its capacity as an advisory body should enable the Center to propose legislation, rules and regulations in order to influence policy on imports and exports of a particular product or a particular industry.

The Requirements for Implementation of the Action Plan

In order to implement the plan of action to provide for a more sustainable position, the Center needs to mobilize its as well as secure other resources to meet its requirements in a number of areas, namely:

- Total computerization of its activities or, at a minimum, computerization of the processing of the claims;
- Preparation of an audit manual and the related instructions;
- Training of the personnel;

The Center needs rigorous training programs for its new hires. We have already discussed this issue in detail in our technical reports. The new hires represent more than 50% of the total employees. There is obviously a need for training of the new hires as well as the continuing training of all the staff.

- Compilation of statistics and information on the claimants;
- Formulation of reporting procedures, and issue of comprehensive information and statistics relating to the type of claimants and the claims, in addition to the information currently produced.

3. MONITORING AND EVALUATION/MANAGEMENT INFORMATION SYSTEM

The objective of this task was to set up systems that would help the Government to predict the likely outcomes of the policy reform and monitor actual performance against those expectations. Policy implementation is likely to be more effective if the intended impacts of the reforms are systematically monitored and responsibilities for responding to non-performance or unintended outcomes are clearly established. At the beginning of the project we were informed by PIDS and other local economists that there had been very little systematic monitoring and evaluation of policies in the Philippines. The components of the system were to be a set of clear objectives for the policy reforms; an analytical framework; and an assignment of responsibilities for using and maintaining the system.

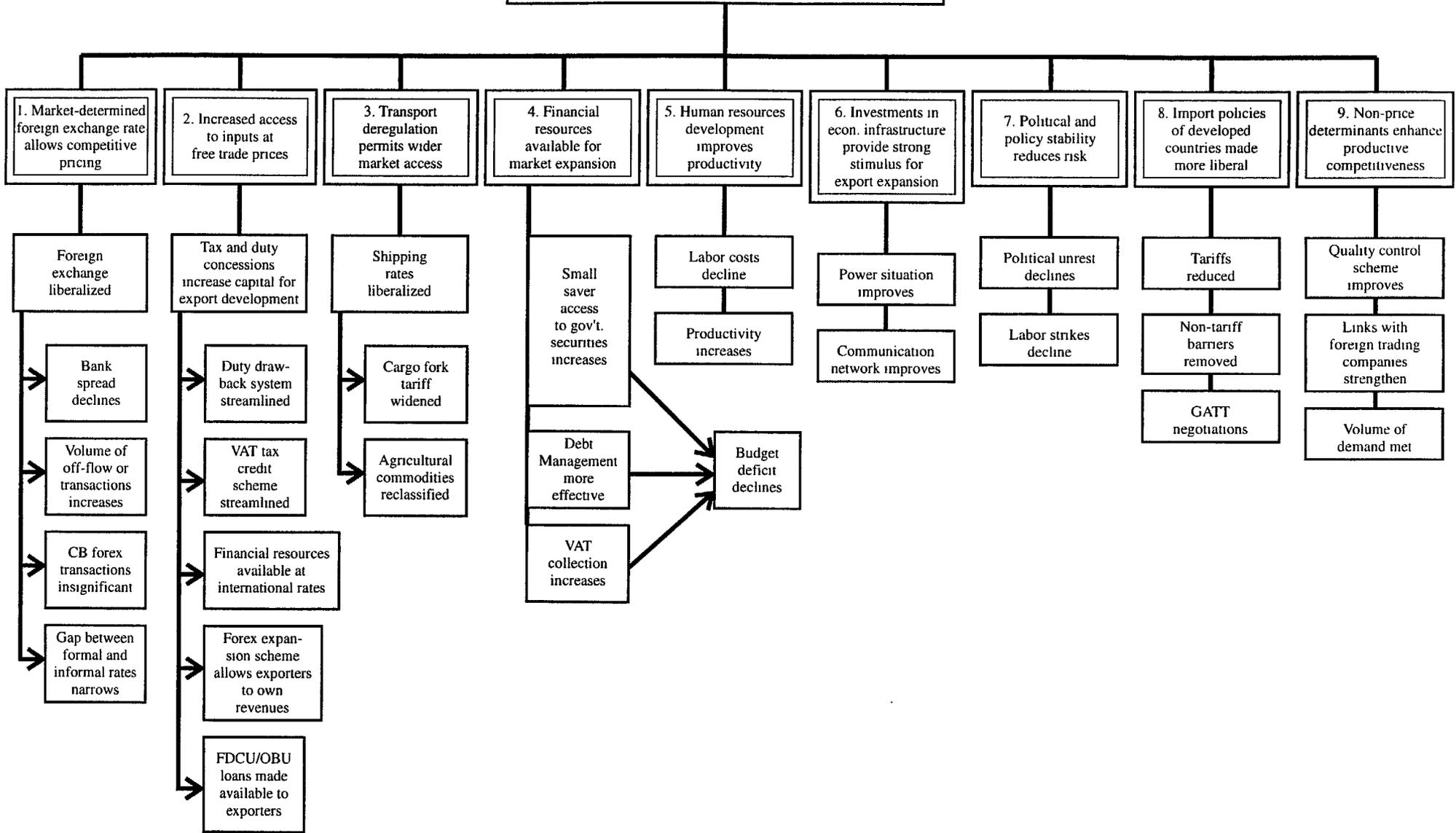
In working on these tasks the IPC team consisted of an expatriate MIS expert, an expatriate economist, two Filipino economists and one Filipino development management expert working with staff from NEDA National Policy Division and the Department of Finance.

The objectives of the system were set out in the form of the objective tree shown in Figure 1. The overall objective is "Philippines Exports Competitive in World Markets," as shown at the very top of the tree. The first four branches on the left had side of the tree are the second level objectives taken from the SDP II Policy Matrix. They answer the first "How to?" question of an objective tree. In other words, to make Philippines exports competitive it is necessary to achieve a market determined foreign exchange rate; improve exporter access to inputs at free market prices; deregulate interisland shipping tariffs so that trade can flow more freely between islands; and make financial resources more freely available. Other factors supporting the achievement of the overall objective, but which were not part of the SDP II Policy Matrix, appear on the right hand side of the tree. The "how to?" questions continue to be answered progressively down the tree from these second level objectives. The tree was drafted by the IPC team and later refined to incorporate the comments of NEDA staff.

On the basis of this tree, the NEDA through the National Planning and Policy, Trade, Industry and Utilities, Agriculture and Infrastructure staffs prepared a matrix showing refined indicators of performance, the agency generating the data and the frequency of data collection.

The objective tree is itself the basis for the analytic framework. Each of the boxes on the table has an associated objectively verifiable indicator of performance, in some instance many of them. Taking the highest level objective first, the team decided that the Government should aim for a neutral trade regime, favoring neither exports (as some Asian governments have done) nor imports (as the Philippines has done in the past with an over-valued exchange rate). This means that the effective rate of exchange for imports must be the same as the effective rate for exports. The equality of these two rates is the indicator. Moving further down the tree to give another example, a series of indicators were designed by the Duty Drawback team to measure the achievement of "streamline duty drawback system." They included progressively higher targets for the time taken to turn around requests for duty drawbacks and more exporters applying for the rebates. The achievement of some of the objectives is difficult to define in terms of an indicator, for example, "political unrest declines." (See Annex 4 for Complete MIS Matrix.)

Philippine Exports Competitive in World Markets



The decision tree itself raises the issue of "manageable interest." Those in government directly responsible for achieving the overall objective, export competitiveness, DOF and NEDA (our principal counterparts), can only be said to have direct responsibility for the achievement of some of the objectives or part of the tree. In general they would take principal responsibility for the left hand side of the tree, the SDP II related reforms. However, since the performance of those reforms will be affected by the factors shown in the rest of the tree, DOF and NEDA have to at least have a "watching brief" over these factors and have to know where to go and who to talk to if it is believed that poor performance is caused by a development outside their control. For example, looking at the "improve export quality" box on the far right hand side of the tree, if information is suspected that exports are not performing up to standard because of poor quality (say, because embassies and the Exporters Council are collecting data on overseas customers' opinions of the quality of the goods and service they buy), then DOF/NEDA need to know where to go to improve matter--probably the Exporters Council itself.

The Filipino team also made use of the 1992 Annual Macroeconomic Model which is an important component of the MIS work under this project. This same model which has been used in the design of the SDP II Policy Matrix to predict the likely outcomes in terms of GDP and sectoral growth, has been modified from the 1989 version in the following ways: the base year was changed from 1972 to 1992; some new definitions and concepts were introduced; improved measurement methodologies were developed; and revised and updated data were utilized. Such a model was required because of the complex interactions between the variables in the analytical framework.

The 1992 Annual Model and the supplement done by the SDP II team are described in one of the outputs of the IPC support, a paper by Eduardo Gonzalez, Mario Lamberte, and Josef Yap, "A Framework and Methodology for Monitoring and Evaluating Export Performance," August 1993. The model consists of 76 equations and a number of identities covering the production, expenditure, prices, wages and employment, fiscal, external and balance of payments sectors. In terms of the model, the level of exports in each sector is expressed as a function of the ratio of costs to the nominal exchange rate (since higher costs that would harm export performance could be offset by a devaluation of the peso), world economic activity levels, and the real value of the flow of credit to deposit money banks. Since the objective is to estimate the impact of the reforms on the cost structure of export firms and then translate that impact to the economy as a whole through changes in the aggregate price indices, Input-Output tables had to be used to achieve the micro-macro interface. In other words input-output analysis was used to estimate the impact of the reforms on costs and prices in five export sectors--garments, semiconductors, agriculture, other manufactures and other exports--and the macroeconomic impact of those price changes was then simulated in the macro model. The principal SDP II induced cost reductions include measures to reduce import costs and transport costs, in particular interisland shipping, taxes and credit costs.

Simulations using the model indicated that the SDP II reforms should have a strong and beneficial impact on the economy. The expected decline in exporters' costs could increase GDP by as much as 3.9 per cent over the baseline case and exports by as much as 5.7 per cent.

An MIS requires the assignment of responsibilities for running and maintaining the macro model, for monitoring performance against all the indicators in the framework or objective tree, and for either taking action in response to information provided by the system or making sure the appropriate organizations and persons do so.

NEDA has clear responsibility for the model, with technical support from PIDS, as needed. Many NEDA staff already knew how to run the previous PIDS/NEDA model. Further work will be required to finalize and institutionalize the M&E framework, for which the matrix in Annex 4 is a beginning. Hands on training on the revised model has not yet been implemented.

The TRP and SDP II taken together have been first steps in an MIS to measure export performance. These steps included policy objectives identification of objectively verifiable indicators of performance and identifying major responsibilities on data collection, integration and analysis. Constructing a composite macro-micro model to evaluate export performance was a significant breakthrough that permitted the linking together of, and analyzing the interaction among, the major economic and fiscal elements necessary for the assessment of export gains. The composite model allows inferences to be made with respect to the course of changes in specific variables (e.g., changes in export levels) in response to specific policy interventions (e.g., currency devaluation). The next critical phases of the MIS (in order to complete the M&E cycle) have yet to be fleshed out. These include the pinpointing of bottlenecks, the identification of corrective action, and policy adjustments. These processes cannot begin until the system is installed. In addition, NEDA has asked that the IPC team submit more detailed documentation to explain the process used to collapse the 426 sectors under the 1985 input-output analysis to 200 sectors. NEDA would also like to have access to the data set used in the input-output computation.

NEDA believes that eventually, a wide area network involving NEDA, BSP, DTI and DOF will be established (at this time, however, NEDA is still waiting for the delivery of new computer hardware and software pledged through a USAID project). There is more or less agreement that NEDA and DOF would assume responsibility for identifying, within their own MIS setups, "flashpoints"--those which are likely to cause bottlenecks if something goes wrong in the system. For instance, foreign exchange, because of its centrality in an export-led economy, will continue to dominate considerations of Philippine trade policy, and will have to be monitored closely. For NEDA, it is clear that NPPS would navigate the system internally and alert decision-makers on any trouble ahead. Director Templo seems to stress that corrective action will have to be tackled at an interagency level, and suggests that Cabinet Clusters A and B, consisting of cabinet secretaries with economic and financial portfolios, would be the proper apparatus for undertaking remedial measures, and "echoing" the corrections back to their respective departments for enforcement or compliance. Cabinet-level decisions mean that the M&E should be adjusted to include informed judgments on the range of political and administrative feasibility of the policy measures being adopted. There is a clear need to allow for risk and uncertainty. For these cabinet clusters, the real choice is not in employing agency resources between the export sector and other sectors, but rather between giving the export sector the differential attention it deserves and leaving it to reactive responses.

Many of the data elements are already being collected by NEDA, and many more are already in the hands of the Bangko Sentral ng Pilipinas and the Department of Trade and Industry. Problems of disaggregation, frequency of collection and reconciliation of figures, could be settled through the National Statistical Coordinating Board, or NSCB. Since the 1992 Annual Macroeconomic Model is a spin-off of an already existing model, the NEDA staff will certainly be able to accommodate the export model in their setup. It is also not difficult to establish both the starting point for the analysis and to set the allowable range over which the model equations would hold. The basic ingredients for institutionalizing the system are available.

Not all components of the framework can be incorporated in the model. Examples include "quality control" and "decline in political unrest." These are best measured in a qualitative, feasibility-type assessments. Responsibilities for detecting potential blockages along these branches of the objective tree are also somewhat more diffuse. The analysis of whether products are of export quality can be given to DTI, which does exercise regulatory influence over export firms. Quality control data collection can be coordinated through existing interagency mechanisms, such as the Export Council, or through a private association, such as PhilExport. But these arrangements remain to be worked out. Gathering the social and political indicators, on the other hand, will require an even broader accommodation with non-economic agencies, such as the National Unification Commission, or the Department of National Defense.

In the end, making social and economic sense out of the framework will require wider inter-agency collaboration. The "export monitors" (NEDA, DOF, DTI, BSP) will still have to sit down together and discuss the allocation of M&E functions. But they are not mandated to deal with political issues impinging on export performance. Other agencies would have to be involved. A cabinet-level export performance monitoring council could offer some distinct advantages over an agency-based MIS.

NEDA could commission impact studies on export, in the context of all the elements in the "objective tree." In addition to economic studies, political economy assessments could be undertaken by research institutions, such as the Philippine Institute for Development Studies, the UP Economics Foundation, the UP College of Public Administration and the Center for Research and Communication.

In fulfilling the monitoring and evaluation component of the project a number of strategic management activities were undertaken, in addition to the specific technical inputs described above.

Strategic Management

In the project period from March 1992 to April 1994 the Implementing Policy Change project provided technical grants for the conduct of strategic planning workshops for senior officials of the Department of Finance and for technical staff of two undersecretaries.

On June 20-21, 1992 outgoing Finance Secretary Jesus Estinaslao and other senior officials underwent a strategic workshop-retreat at Corregidor, facilitated by IPC Consultants Janet Tuthill, Dr. Alice Morton, Norman Bramble and Gabriel Lopez. It was an opportunity to put to useful

application some strategic management tools developed by IPC Consultant Dr. Benjamin Crosby for the IPC Project worldwide. These included a simplified scan of the Philippine economy's environment to identify opportunities and threats, as well as an identification of the various stakeholders involved in key policy areas, and a review of their interests and positions vis-a-vis such policies.

Given the brevity of the retreat hours, the program syllabus was modified to accommodate key observations and suggestions, particularly from the outgoing Secretary and an observer team from the incoming administration. The four areas of strategic importance that became the focus of strategizing and action planning were: mobilization of funds for National Government expenditures; prioritization of National Government expenditures and assistance; financial stability; and agro-industrial development. A group was tasked to work in each of these four areas. Each group focused on developing specific objectives and the identification and discussion of strategies and policies that would lead to the accomplishment of the objectives. Based on this exercise, each group developed actions plans for carrying out a number of the key actions including: increasing revenue generation; reducing fiscal incentives; increasing capital expenditures; restructuring domestic debt; finalizing the economic program and debt package with foreign lending institutions; finalizing a small savers' plan; and the promotion exports and investments.

On February 27-28 1993, the new Finance Secretary, Ramon del Rosario and other senior officials of the Department of Finance participated in a strategic planning workshop in Lake Caliraya, Laguna to address strategic issues in three key areas of concerns: revenue mobilization; financial management; and, local government finance and government corporations' operations. The revenue mobilization group identified three strategies with detailed action plans. These were: maximize revenue collections/minimize erosion of revenues; maximize revenue collections/widen revenue base; and improve the quality of expenditures. The financial management group identified policies for improving external financing; improving domestic financing; improving cash management; development of capital markets; privatization of government corporations; expanding market for government securities; and issuing long-term bonds. The local government units group developed action plans for: developing a scheme for financing devolution; arriving at the final definition of basic income for IRA; and standardizing property values for taxation and other governmental purposes. The government corporations group did not complete actions plans but identified the following strategies: improve financial viability of GOCCs; establish definitive policies for the existence of GOCCs; retain GOCCs involved in sustainable developmental activities; establish a consistent policy for monitoring and evaluating GOCC performance; and, adoption of a differential treatment policy from service wide agencies with regard to performance incentives, accounting and auditing and staffing patterns.

In April 1993 Finance Secretary Ramon del Rosario's permanent appointment was bypassed by the Philippine Congress' Commission on Appointments. To replace him on an interim basis, Finance Undersecretary Ernest Leung was appointed by the President. During Secretary Leung's interim administration, there was limited support for the activities of IPC-SDP II Project, including the continuation of strategic management. Secretary Leung was replace by a new Secretary in mid-February 1994. The new Finance Secretary, Roberto de Ocampo is supportive of the IPC-SDP II Project activities, including strategic management.

The technical assistance grant to the Department of Finance for a final top-level strategic planning workshop before the end of the project period was re-allocated to two separate strategic planning workshops, one each for the group technical staff of Undersecretary Romeo Bernardo and Undersecretary Juanita Amatong.

On February 25-26 the technical staff of groups managed by Undersecretary Romeo Bernardo (International Finance, Domestic Finance, and Privatization) had a strategic planning workshop in Subic, Zambales facilitated by IPC Consultant Gabriel Lopez. There were 28 technical staff who participated. The three principal areas with strategic issues that were addressed were: human resources development, organization effectiveness, and public affairs.

On March 22-23, 1994 the technical staff of the Department's Policy Development and Management Services Group under Undersecretary Juanita Amatong had a strategic planning workshop at the Department's Jaime V. Ongpin Training Center facilitated by IPC Consultant Gabriel Lopez. There were 12 participants and the two principal areas of strategic concern were: human resources development and institutional/organizational effectiveness. The human resources development group identified three strategies to improve the human resources in the department. These included: the recruitment and hiring of new personnel, the development and implementation of a continuous training program for new and existing staff, and the provision of recognition and incentives to the staff. The organizational effectiveness group focused on three strategies addressing the key issues facing the group: realigning existing plantilla/personnel into a more effective organizational and functional structure; enhancing coordination among DOF offices and between the DOF and other offices/agencies; and, upgrading office facilities and equipment. The public affairs group also identified three actionable strategies: launch an aggressive DOF policy information campaign; strengthen liaison with congressional counterparts; and reactivate the press office.

Strategic management has been accepted at the Department of Finance as a consequence of the technical support of the IPC Project. The Department is well on its way to institutionalize strategic planning on a regular/annual basis for all its groups. The new Finance Secretary has decided to hold a top-level strategic planning workshop, even after the end of the IPC Project. Undersecretary Amatong also has decided to hold strategic planning workshops for the technical staff of two other groups under her management.

4. STRENGTHEN VAT ADMINISTRATION

This Task primarily relates to the VAT credit activity. There is limited reference in the scope of work for the provision of technical assistance relating to the VAT administration, in general. Nonetheless, the refund process represent an integral part of the VAT, as a tax collection system, as a whole. We, therefore, carried out a full review of the VAT legislation and VAT implementation in the Philippines.

Strategic Management: On November 5 - 6, 1993 IPC Consultants Nezam Motabar and Gabriel Lopez conducted a strategic planning workshop on improving VAT administration as well as the overall operations of the Bureau of Internal Revenue. The workshop was held at the Development Academy of the Philippines in Tagaytay and was attended by 18 senior Bureau officials, including BIR Commissioner Liwayway Vinzons Chato and her deputy commissioners, assistant commissioners and other senior managers. In addition, three consultants from the U.S. Internal Revenue Service (IRS) attended as observers. The most significant outcome of the workshop as far as improving VAT administration was concerned was an agreement and plan to decentralize and devolve the functions of the VAT Distribution to the Revenue District Offices (DSOs) by February 1994.

Training: On November 18 - 22, 1992 IPC Consultant Nezam Motabar accompanied five senior managers of the BIR VAT Division led by the Division Chief to observe VAT administration practices in Jakarta, Indonesia.

Study and Review: IPC Consultant Nezam Motabar provided specific technical advice to the VAT Division in May and November 1992 and in February, July and November, 1993. The results of his work are included in technical project reports. Future directions are summarized below. Details of each intervention are provided in specific reports.

Performance Report: As far as VAT services impacting exporters are concerned, the processing of the entire VAT refund for exporters was transferred to the One Stop Shop Inter-Agency Tax Credit and Duty Drawback Center from the BIR VAT Division by virtue of Revenue Audit Memorandum Order (RAMO) No. 2-93.

Observations: The abolition of the VAT Division and the devolution of its functions and powers to the RDOs is a positive development because it makes easily available and accessible VAT-related services to more taxpayers throughout the country. It is expected to decllog the BIR Central Office of VAT-related matters, including applications for exemptions, reductions and adjustments.

As part of our work, we prepared an inception report containing general observations on the scope of work as it related to strengthening VAT administration. We have also submitted a technical report (June 1992) on the VAT administration. The latter report provides a review of the VAT legislation and its implementation as compared to the VAT as a tax collection system in general. The report provides for revisions in certain areas. The report did not address changes to the VAT law as the terms of reference related to implementation issues.

As a result of the decentralization of the BIR, and also the efforts made under the SDPII project, as a whole, the actions set out below have been taken or are being considered. These actions to a large degree reflect the same issues which have contributed to the success of the VAT system as it is functioning in Indonesia.

- Transfer of the VAT credit processing to the Center. This action should also be evaluated in the light of recommendations proposed by the management audit of the BIR, and more importantly the decentralization of the activities of the BIR (as the major single factor);
- Proposal by the VAT Division to the BIR for the possible introduction of the standard VAT invoice system similar to the one in operation in Indonesia and other countries in the region.

As we have already mentioned, the refund process is normally an integral part of the payment process. This is particularly true with respect to the VAT system. Computation of the VAT payment or the refund is the result of the difference between two elements: 1) the input tax, and; 2) the output tax.

If the output tax is more than the input tax, it results in a payment by the taxpayer representing the difference. Otherwise, there is a refund due to the taxpayer. Therefore, in fact there is little difference in terms of processing between a VAT payment and a VAT refund. It is due to this particular characteristic of the VAT system, that we have always maintained that to strengthen the VAT credit system one has to consider a global approach to the whole VAT system.

In general there is still a need for technical assistance in the VAT collection area. We consider that there is a considerable amount of scope for an increase in the rate of collection of the VAT without any change in the current VAT base and coverage. Recent legislative changes might provide opportunities for further streamlining.

5. CONCLUSIONS AND OPPORTUNITIES

This section will focus on opportunities and potential constraints related to each of the project components.

5.1 Streamline Duty Drawback and VAT Tax Credit

The Center is operational and processing credits at a rate that complies with the original SDP II targets. The staffing levels currently allow adequate operations but will need to be closely monitored to ensure that the necessary human resource levels are maintained to process what may become an increasing demand for tax certificates. Throughout the period of assistance under SDP II the staffing levels have been an issue and while the GOP is well aware of this need, senior DOF, BOI and BOC managers will need to continue to monitor staff levels.

The Center has organized itself around the regulations governing the refund process. It has been developing its own procedures to replace those that were specific to the organizations which originally handled the actions. Continued progress in this area would be beneficial to increasing efficiency over time. To this end continued progress in automation of processing will also yield database information with which to track performance and attribute tax credits to specific sectors more easily.

Equipment is in place, but more will be needed as the activities are increased and more of the day to day work becomes automated. GOP attention to providing adequate equipment will be important in ensuring Center sustainability.

The strategic management process through workshops and retreats seems to have taken hold and to be used extensively by the agencies involved in the operation of the Center as well as by DOF senior decision-makers. Sufficient iterations of the process were implemented during the project to allow for replication by the DOF when desired. Throughout this process the Philippine-based team placed special emphasis on transferring the elements of the strategic planning to the participants in the process.

We suggest that the elements of the plan of action for the Center outlined in section 2.2 of this report be reviewed by key GOP decision-makers to see if any of the steps could be planned for in the near future. Since the revenue loss in the short term is likely to continue to be an issue for the GOP, the consideration of both a longer term and medium term policy for export promotion including tax credits may be needed.

Since a large amount of time and resources under the project have been devoted to the work of the Center and more is currently known about how to move from current progress to future action, it seems likely that attention devoted there can yield strong long term results.

5.2 Monitoring and Evaluation/Management Information System

The work on this component focused on setting up systems which would allow the GOP to predict outcomes of the policy reforms under SDP II and to monitor performance against

expectations. Using an objective tree and accompanying indicator matrix (See Annex 4), the team developed a more comprehensive view of both what it takes to monitor improvements in the export sector and what other variables influence these outcomes. This analytical approach which was developed with extensive input from NEDA allows for a less restricted view of performance in the sector.

As noted earlier, the PIDS/NEDA Annual macroeconomic model updated under this project forms an important part of MIS. The current version responds to the present needs of NEDA for policy analysis and planning. The GOP can make use of it as needed to predict and monitor some important aspects of export performance.

Simulations using the model indicate that SDP II reforms should be beneficial to the economy with declines in exporters costs increasing GDP 3.9% over the baseline case. Exports could increase by as much as 5.7% as a direct result. The model is under the responsibility of NEDA who have staff who can be trained to run it when needed with technical support from PIDS if necessary. Official adoption of both the framework and model have been proposed to NEDA. The procurement of additional equipment through another USAID project will assist in this implementation.

The importance of certain key variables in the equation such as foreign exchange requires government-wide monitoring beyond the scope of SDP II. Risk assessment in decision-making is central to successful use of the information.

The team found that the basic elements for institutionalizing the MIS are already present. The GOP is invited to assess the value in using this conceptual and information framework as a starting point for a more comprehensive attempt to monitor progress in this sector. A set of guidelines for the process are included in the team's final MIS product. NEDA with support from PIDS will need a detailed operations manual for the MIS. Reduced resources for this component did not permit its completion under the SDP II funding for IPC.

5.3 Strengthen VAT Administration

During implementation it proved difficult to artificially separate the actions on VAT credit from the overall VAT administration improvements which were indicated in the scope of work but not detailed. In the report it will be noted that although reporting on the VAT administration as a separate activity is more limited, large amounts of assistance were provided to VAT functions through the assistance to the Center. Indeed, without active work and consultation with the BIR throughout, progress on the streamlining of Center activities could not have been made.

Significant achievements include the transfer of VAT refund for exporters to the Center, strategic planning for decentralization and specific technical reports provided on operations.

Options for consideration are the introduction of a standard VAT invoice system similar to the one observed in Indonesia and improvements in VAT collection. These have been outlined in technical products produced for the VAT administration and require a more global approach to the whole VAT administration.

5.4 Strategic Management

Strategic management has been accepted at the Department of Finance as a result of this project. They are likely to continue using strategic planning annually for all their units. Plans are already made to conduct sessions after the project. The BIR used the strategic management approach successfully in clarifying its VAT priorities. It could usefully implement some strategic management in improving its VAT collection in the future. Specific strategic management interventions could be designed to assist VAT in this effort.

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ANNEX 1

Scope of Work

A six-day work week without premium compensation is allowed.

Article VI - Performance Period

February 1992 - August 1993

Article VII - Personnel Requirements and Level of Effort

The following qualifications are needed, including an estimate of the number of workdays per position:

| <u>Position</u> | <u>Workdays</u> |
|---------------------------------------|-----------------|
| 1. Senior Policy Change Specialist(s) | 290 |
| 2. Management Specialist(s) | 100 |
| 3. Technical Expert(s) | 480 |
| Total | 870 |

The candidate(s) for each position should have at least a Masters degree appropriate to the applied position, preferably a Ph.D., complemented by at least seven years of relevant and applied research and consultancy work. The individual candidates should have adequate developing country research and consultancy experience. The team as a whole should have extensive Philippine background and particular experience on duty drawback operations, VAT credit administration and establishment of the MIS.

Article VIII - Illustrative Budget

See Attachment No. 1.

Article IX - Additional Provisions

A. Duty Post

Manila - 85 percent of total work time; other cities such as Davao and Cebu - 5 percent of total work time; and in headquarters - 10 percent.

B. Logistic Support

The consultants shall be responsible for logistic support.

ANNEX 2

**Short-Term Overseas
Technical Assistance Provided
IPC - SDP II**

**Short-Term Overseas
Technical Assistance Provided
IPC - SDP II**

| DATE | TEAM MEMBERS | PURPOSE |
|--|--|---|
| March 1992 JT: March 16-April 3 HG: March 18-April 3 CK: March 22-April 25 BC: March 28-April 9 AM: March 14-22 NM: March 16-April 3 | Ben Crosby, Harry Garnett, Chip Krakoff, Harry Garnett, Chip Krakoff, Alice Morton, Nezam Motabar, Janet Tuthill | To assist the Government of the Philippines in strategic management of implementation activities to achieve objectives in the Support for Development II project policy matrix. |
| May 1992 JT: May 27-June 16 HG: May 27-June 10 NM: May 28-June 18 | Janet Tuthill, Nezam Motabar and Harry Garnett | To continue to support the GOP in AID's SDPII program. |
| June 1992 June 9-23 | Alice Morton | To provide additional technical assistance to the One Stop Shop for Duty Drawback and the VAT Credit System of the Bureau of Internal Revenue. |
| September/October 1992 Sept. 27-Oct. 9 (includes study tour below) | Chip Krakoff | To finalize the observation/study tour for the GOP staff involved with the operations of the One Stop Duty Drawback Center. |

| DATE | TEAM MEMBERS | PURPOSE |
|--|----------------------|---|
| <p>October 1992 Oct. 3-9</p> | <p>Chip Krakoff</p> | <p>Traveled to New Zealand with five members of the GOP to observe and study the Duty Drawback Operations of the New Zealand Customs Service. GOP team included: Mr. Uldorico P. Andutan, Jr. (Department of Finance (DOF)); Mr. Raul C. De Vera (DOF); Mr. Teodoro L. Cinco (Bureau of Customs); Mr. Carl John G. Matriano (Board of Investments); and Mr. Ricardo A. Santos (Bureau of Internal Revenue).</p> |
| <p>October/November 1992 Oct. 23 - Nov. 7</p> | <p>Alice Morton</p> | <p>To participate in the Duty Drawback six month evaluation and decentralization study and to help with the design of the exporter surveys which are part of the overall MIS.</p> |
| <p>November 1992 Nov. 14 - Dec. 5 Includes Study tour to Indonesia: Nov. 17-22</p> | <p>Nezam Motabar</p> | <p>To plan and conduct an observation/study tour for five BIR-VAT officials to Jakarta of operations of the Indonesian Vat System as part of the continuing engagement to improve implementation of the Bureau of Internal Revenue-Value Added Tax (BIR-VAT) System.</p> <p>To attend a strategic planning VAT meeting in Manila.</p> |
| <p>February 1993 Feb. 22-24 merely a stopover</p> | <p>Harry Garnett</p> | <p>To review progress on the Management Information System for SDP II.</p> |
| <p>July 1993 approx. 22 days starting o/a July 4</p> | <p>Nezam Motabar</p> | <p>To advise the Bureau of Internal Revenue of the GOP on regionalizing and decentralizing VAT administration and incorporating tax credit activities in the Duty Drawback Center.</p> |

| DATE | TEAM MEMBERS | PURPOSE |
|---|---------------------|--|
| October/November 1993 Oct. 24-Nov. 7 | Nezam Motabar | To assist the Duty Drawback Center with streamlining procedures for VAT refund processing, identify areas at the Center needing capability building and participate in the BIR-VAT workshop. |

ANNEX 3

Reports List

Technical Reports Produced by SDP II IPC Project

Accomplishment Report: One-Stop Inter-Agency Tax Credit and Duty Drawback Center. December 31, 1992.

Annual Report: One-Stop Shop Inter-Agency Tax Credit and Duty Drawback Center. May 1992 to April 1993.

Bramble, Norman R., Guia L. Espiritu, Report on the Strategic Planning Workshop of the Department of Finance's One Stop Shop - Duty Drawback Center. Manila; March 21, 1994.

Crosby, Benjamin, One-Stop Shop Interagency Tax Credit and Duty Drawback Center: The Strategic Management Process. Philippines; May 1992.

Garnett, Harry, SDP Support Services: Economic Analysis and the Use of Models in the Monitoring and Evaluation System. Philippines; June 3, 1992.

Garnett, Harry, Alice Morton, Pat Isman IPC in the Philippines: The Support for Development II Program. October 10, 1991.

Garnett, Harry, Monitoring Economic Policy Reform Programs: Export Competitiveness Policy in the Philippines.

Garnett, Harry, Eduardo T. Gonzalez and Janet C. Tuthill, MIS Guidelines, May, 1994.

Gonzalez, Eduardo T., Mario B. Lamberte, Josef T. Yap, A Framework and Methodology for Monitoring and Evaluating Export Performance.

Krakoff, Charles E., Report of Philippines Duty Drawback Center New Zealand Study Tour. October 1992.

Krakoff, Charles E., Duty Drawback Center: Preliminary Automation Specifications. Philippines; April, 1992.

Krakoff, Charles E., One-Stop Shop: Project Implementation Issues. Philippines; April 1992.

Krakoff, Charles E., Streamline Duty Drawback and VAT Tax Credit System: Technical Report. Philippines; April 1992.

Lopez, Gabriel J., Report on the Strategic Planning Workshop of the Department of Finance's Policy Development and Management Services Group. J.V. Ogpin Training Center Department of Finance; March 22-23, 1994.

Report on the Strategic Retreat-Workshop for Senior Executives of the Department of Finance.
July 2, 1992.

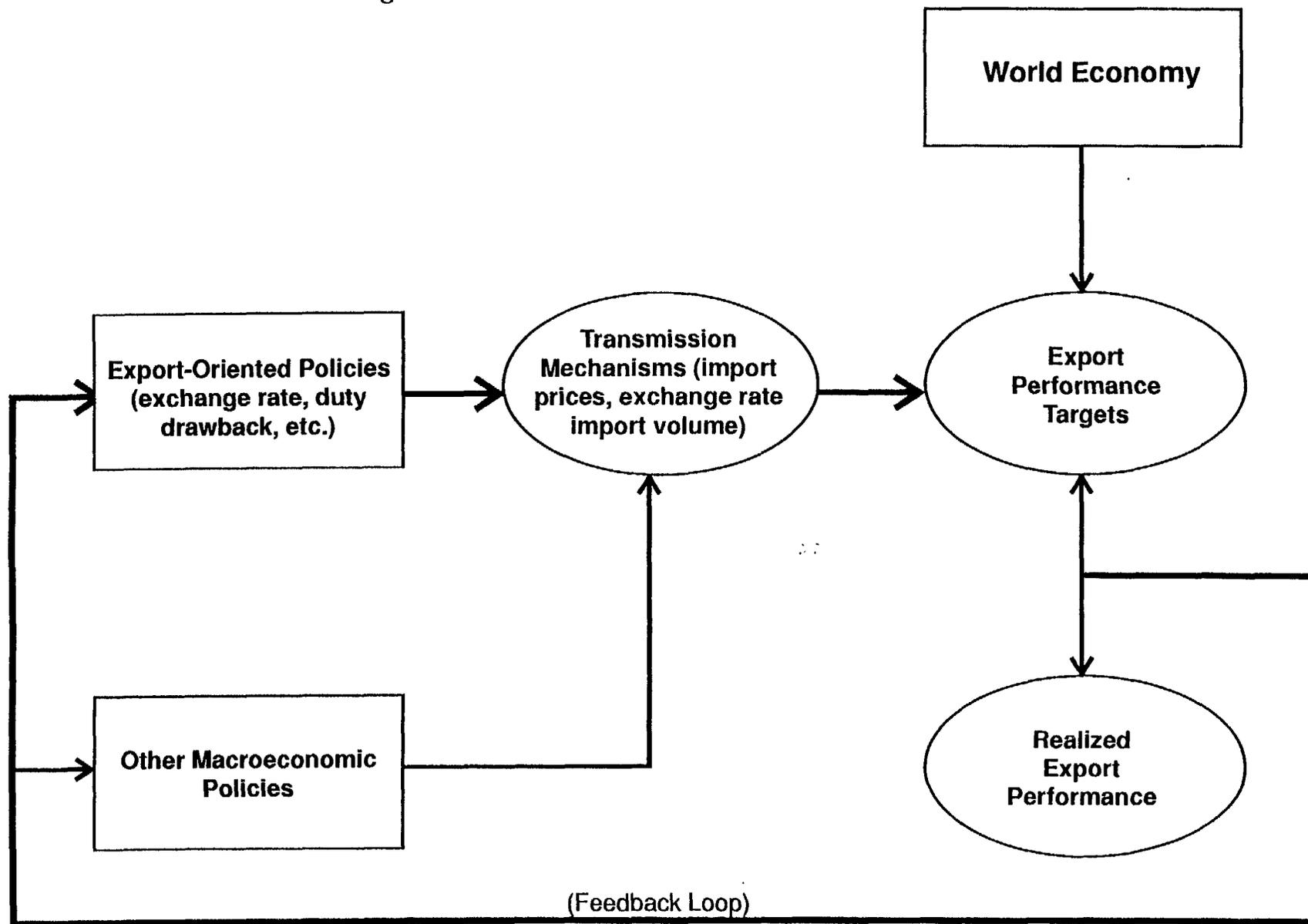
Report on the Workshop: Team Building, Values Formation and Operations. Department of
Finance, Manila; June 7-11, 1993.

ANNEX 4

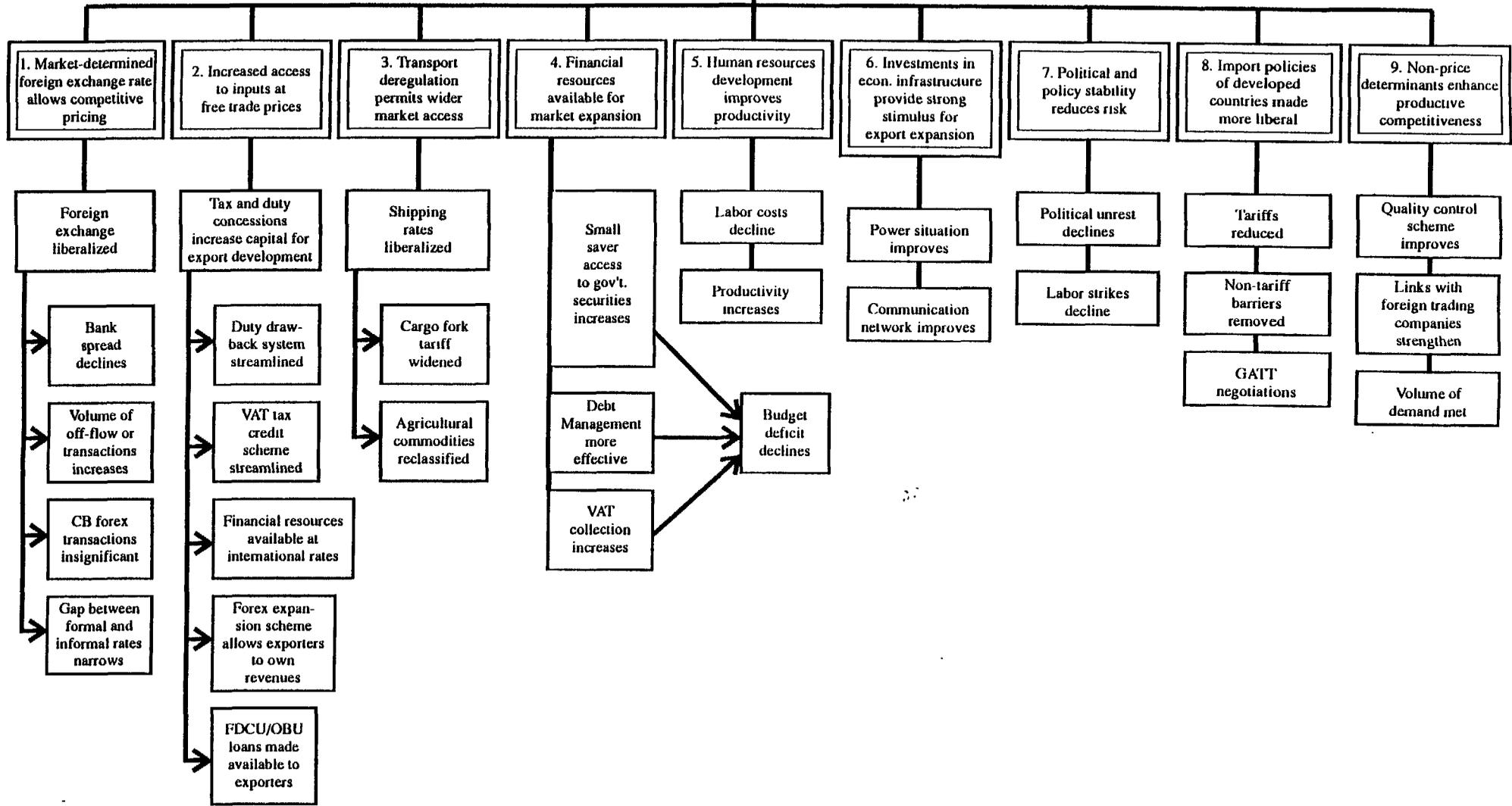
MIS Objectives and Matrix

Figure 1

Monitoring and Evaluating Exports
Using the PIDS-NEDA Macroeconometric Model



Philippine Exports Competitive in World Markets



Support for Development Program II
Matrix on the Proposed Refined Indicators of Performance

Overall Objective: Philippine Exports Competitive in World Market

| Policy Level | Transmission Mechanisms | Proposed Refined Indicator of Performance | Data Source (i.e., agency producing the information) | Frequency (e.g., daily, weekly, monthly quarterly, etc.) Base year (if available) |
|--|---|--|---|---|
| I. Market-determined foreign exchange rate allows competitive pricing A) Foreign Exchange liberalized | Bank spread declines | Difference between buying and selling rate of forex | Bangko Sentral ng Pilipinas (BSP), KBs | daily |
| | Volume of off-floor transactions increases | Volume of daily FX transactions | BAP | daily |
| | CB forex transactions insignificant | Volume of daily dollar purchases/sales of CB | BAP | daily |
| | | Volume of spot purchases from/sale to KBs | BSP (Annual Report) | annually |
| | Gap between formal and informal rates narrows | Difference between BAP rate and black market rates | BAP, KBs, Money changers | daily |
| II. Increased access to inputs at free trade prices A) Tax and duty concessions export development | | Increase in investments in export-oriented activities attributable to tax and duty concessions | DTI/BOI | |
| | | Increases in availability of working capital due to shift in resource use from tax payments to working capital | PCCI, PHILEXPORT (possible) | |
| | | Duty drawback system streamlined | Reduction in number of steps involved in the processing of applications for duty drawback | DOF |
| | Reduction in the processing time | | DOF | |

SP

| Policy Level | Transmission Mechanisms | Proposed Refined Indicator of Performance | Data Source (i.e., agency producing the information) | Frequency (e.g., daily, weekly, monthly quarterly, etc.) Base year (if available) |
|---|---|---|--|---|
| B) Financial resources available at international rates | VAT tax credit scheme streamlined | Ratio of applications processed to applications filed within prescribed processing time | DOF | |
| | | Number of manpower involved in the processing of applications before and after operations of the Duty Drawback Center (manpower productivity) | DOF | |
| | | Reduction in number of steps involved in the processing of applications for VAT tax credit | BIR | |
| | | Reduction in the processing time | BIR | |
| | Formula of manufacture for priority export items standardized | Standard formula for 200 priority export items updated | ITD/NSTL | |
| | | Number of export items for which SFM will be developed is increased | ? | |
| | | Ratio of applications processed to applications filed within prescribed processing time | BIR | |
| | | Number of manpower involved in the processing of applications before and after operations of the Duty Drawback Center (manpower productivity) | BIR | |
| | Market information made more available | Number of information dissemination projects implemented | DTI-BETP, PITO-P | |
| | | Number of exporters availing of data thru CTIS, PITO-P and other information systems/networks | DTI-BETP, PITO-P | |
| | Libor declines | BSP | | |

| Policy Level | Transmission Mechanisms | Proposed Refined Indicator of Performance | Data Source (i.e., agency producing the information) | Frequency (e.g., daily, weekly, monthly quarterly, etc.) Base year (if available) |
|---|--|--|--|---|
| III. Transport deregulation permits wider market access A) Shipping rates liberalized | Forex retention scheme allows exporters to own dollar revenues | Outstanding balance of Special Foreign Currency Deposits Accounts (SFCDA) | MB and BSP (Report on Export Negotiations; Report on SCFDA opened, closed and outstanding balance during the report month) | monthly |
| | FCDU/OBU loans made available to exporters | Amount of FCDU loans granted to exporters | MB and BSP (Report on Export Negotiations) | monthly |
| | Cargo fork tariffs widened | Order/memorandum issued by MARINA to widen cargo fork tariff from the prevailing +/-5 percent (This has been effected with the issuance of Memorandum Circular No. 67 issued by MARINA on 6 May 1992 which provides for the adoption of a -10/+15% fork tariff and to be implemented in January 1993.) | | |
| | Agricultural commodities reclassified (shipping rates for agricultural commodities are made competitive with non-agricultural commodities) | Increase in the percent share of quantity and value of coastwise trade of agricultural commodities to total quantity and value of coastwise trade of all commodities | NSO | annually |
| B) Shipping routes liberalized | Entry/routes deregulated | Increase in the quantity and value of coastwise trade of agricultural commodities | NSO | annually |
| | | Increase in number of operators/route | MARINA | |
| IV. Financial resources available for market expansion A) Small saver access to government securities increase | | Decline in port handling charges/tumaround times | MARINA | |
| | | Formation of mutual funds or unit trust accounts investing exclusively in government securities (To be provided by the consultants) | DOF-DOG | |

| Policy Level | Transmission Mechanisms | Proposed Refined Indicator of Performance | Data Source (i.e., agency producing the information) | Frequency (e.g., daily, weekly, monthly quarterly, etc.) Base year (if available) | |
|-----------------------------------|---|---|--|---|-----------------|
| B) Debt management more effective | | Improvement in the debt burden (foreign and domestic) to GNP ratio | DOF/DBM | | |
| | | Reduction in the interest payments (foreign and domestic) to GNP ratio | DOF/DBM | | |
| | | Reduction in the stock of commercial and official debts (external) | BSP | | |
| | | Reduction in the share of more expensive commercial debt (external) to the total debt | BSP | | |
| | | Lengthening of the maturity structure of outstanding debt (internal and external) | BSP | | |
| | | Privatization program is accelerated | 50% of total assets identified for privatization offered for sale | APT | |
| | | VAT collection increases | Number of VAT registrants increases | BIR | quarterly |
| | | VAT collection increases | Number of VAT filers increases | BIR | quarterly |
| | | VAT collection increases | VAT collection increases in real terms | BIR | quarterly |
| | | VAT/NP ratio increases | VAT/NP ratio increases | BIR | quarterly |
| | | Budget deficit declines | Budget deficit as a percentage of GNP declines | DOF, DBM, NEDA Bureau of Treasury (BTr) | annually weekly |
| | | Budget deficit declines | Budget deficit declines in real terms over time | DOF, DBM, NEDA BTr | annually weekly |
| | V. Human resource development improves productivity | Labor costs decline | Legislated daily minimum wage rates (nominal wage maintains the same level; real wage declines assuming inflation) | National Wages and Productivity Commission | monthly |

df

| Policy Level | Transmission Mechanisms | Proposed Refined Indicator of Performance | Data Source (i.e., agency producing the information) | Frequency (e.g., daily, weekly, monthly quarterly, etc.) Base year (if available) |
|--------------|--|---|---|---|
| | | Index of compensation (manufacturing sector only) declines | NSO | monthly (base year = 19985) |
| | | Index of compensation (for all other sectors except agriculture) declines | National Statistical Coordination Board (NSCB) | quarterly (base year = 1978) |
| | | Agricultural wage rates in farm households maintains the same level | Bureau of Agricultural Statistics | semestral |
| | | Philippine labor cost compared to ASEAN labor cost lower | Yearbook for Labor Statistics, International Labor Office | annually |
| | | Average monthly wage rate of selected occupations in non-agricultural establishments maintains the same level | Bureau of Labor and Employment Statistics | quarterly |
| | | Other non-wage indicators increase | GSIS, SSS, Medicare | monthly |
| | | Reduction in labor costs per unit of output due to HRD | | |
| | Productivity increases | Gross domestic product and sectoral gross value added increase | NSCB | quarterly |
| | | Total employment increase and sectoral employment (for industry - increase; for agri and services - decrease) | NSO | quarterly |
| | | Profit sharing schemes increase | Department of Labor and Employment (DOLE) | as reports come |
| | | Increase in output per unit of manhour | DOLE, NSCB | quarterly |
| | | Increase in productivity bonuses given to laborers/employees | | |
| | Per capita expenditures on essential social services increases | Expenditures on health, nutrition and education as a proportion of total expenditures | DBM | annually |

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| Policy Level | Transmission Mechanisms | Proposed Refined Indicator of Performance | Data Source (i.e., agency producing the information) | Frequency (e.g., daily, weekly, monthly quarterly, etc.) Base year (if available) |
|--|--|--|--|---|
| VI. Improvement in investment climate | Power situation improves. | Per capita expenditure on health, nutrition and education | DBM, NSO | annually |
| | | Power reserve capacity increases | NPC | weekly |
| | | Power generating capacity increases | | |
| | Power cost declines | Power cost as a proportion of total cost declines (production sector) | | |
| | | Philippine power cost compared to ASEAN power cost lower | | |
| | Communication network IMPROVES | Regional/provincial disaggregation of communication indicators - telephone density and area coverage increase - national and international telex and telephone traffic increases - data transmission and equipment traffic increase | NTC/DOTC | annually |
| VI. A. Domestic trade policies made more liberal | Foreign Investment Act Implementation | Level of foreign investments | BSP, SEC, BOI, NEDA | monthly |
| | | Negative list shortened | | |
| | | Debt/equity swap facilities expanded | | |
| | Investment promotion accelerated | BOI converted into investment promotions industry | | |
| | Quantitative restrictions reduced | QRs progressively eliminated | | |
| | Level and dispersion of tariff rates reduced | Number of regulated items | | |
| | | Nominal tariffs | | |
| | | Effective rates of protection | | |

SP

| Policy Level | Transmission Mechanisms | Proposed Refined Indicator of Performance | Data Source (i.e., agency producing the information) | Frequency (e.g., daily, weekly, monthly quarterly, etc.) Base year (if available) |
|---|---------------------------|--|--|---|
| VII. Political and policy stability reduces risks | Political unrest declines | Non-violent elections sustained | Commission on Elections | |
| | | Peace settlements with rightist, leftist and secessionist rebels concluded | National Unification Commission | |
| | | Political amnesty program launched | National Unification Commission | |
| | Labor strikes declines | Capital flight declines | BSP | |
| | | Labor organization indicators - workers organized increase - workers covered by collective bargaining agreements (CBAs) increase | Bureau of Labor Relations | monthly |
| | | Number of strikes decline | National Conciliation and Mediation Board | monthly |
| | | - workers involved - mandays lost | | |
| | | Use of arbitration or peaceful settlement of cases increases | National Conciliation and Mediation Board | monthly |
| | | - preventive mediation | National Conciliation and Mediation Board | monthly |
| | | - voluntary arbitration increase | National Conciliation and Mediation Board | monthly |
| | | - mediation-arbitration | National Conciliation and Mediation Board | monthly |
| | | - arbitration | National Conciliation and Mediation Board | monthly |
| | | Labor management cooperation schemes increase | Bureau of Labor and Employment Statistics | monthly |
| | | Labor education increases | Bureau of Labor and Employment Statistics | monthly |

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| Policy Level | Transmission Mechanisms | Proposed Refined Indicator of Performance | Data Source (i.e., agency producing the information) | Frequency (e.g., daily, weekly, monthly quarterly, etc.) Base year (if available) |
|--|--|--|--|---|
| VIII. Import policies of development countries made more liberal | Tariff on Philippine exports reduced | - seminars/workshops increase - number of participants Compliance to labor legislation, e.g., health standards, minimum wage, occupational safety increase | Bureau of Working Conditions | monthly |
| | Non-tariff barriers removed | Tariff concessions on Philippine exports under GATT, ASEAN, PTA, BAAIJV, and BBC schemes, GSP and GSTP | DTI-BITR, TC, BSP-DEES | |
| IX. Non-price determinants enhance product competitiveness | GATT negotiations | Quantitative (quotas) and non-quantitative (e.g., quality standards) restrictions on Philippine exports lifted | DTI-BITR, BETP, BSP-DEES | |
| | Quality control scheme improves | Partial preferential arrangements | DTI-BITR | |
| | Links with foreign companies strengthens | International standards adopted (benchmarking) | DOST | |
| | Volume of demand met | - Number of rejects decreases | DTI | |
| | | Number of agreements with foreign firms on product design/quality increases | DTI | |
| | | Number of late deliveries decreases | DTI | |
| | | Target quotas filled | DTI | |

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