

Decentralizing Philippine Development

An Assessment of the Decentralized Shelter and Urban Development Program

June 1991

OFFICE OF

HOUSING AND URBAN

PROGRAMS

U.S. AGENCY FOR INTERNATIONAL DEVELOPMENT



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Title: Decentralizing Philippine Development: An Assessment of the Decentralized Shelter and Urban Development Program

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Pub. Date: June 1991
Project #:
Contract #: PDC-1008-I-00-9067-00
Pages: 70
Language: English
Sponsor: USAID/Philippines; APRE/H

Abstract: This study reviews the agenda and progress of the Decentralized Shelter and Urban Development program (DSUD), designed by USAID and the Philippine Government in 1990. DSUD's goals include helping cities to: 1) develop a self-sustaining system of financing; 2) improve the delivery of urban services and infrastructure; 3) improve access to sustainable urban shelter delivery for low-income households. In addition to reviewing the Philippine government's progress in meeting DSUD objectives, the report also examines the broader context and progress of decentralization in the Philippines, focusing on economic change and patterns of urbanization.

Index Terms: Philippines/Decentralization/Urban Development/Local Government/Infrastructure & Urban Services/Municipal Finance & Taxation

Document id:

DECENTRALIZING PHILIPPINE DEVELOPMENT
AN ASSESSMENT OF THE DECENTRALIZED
SHELTER AND URBAN DEVELOPMENT PROGRAM

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June 1991

Report prepared for the
U.S. Agency for International Development
The Philippines

THE URBAN INSTITUTE
WASHINGTON, D.C.

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EXECUTIVE SUMMARY

BACKGROUND AND PURPOSE

In September 1990, the U.S. Agency for International Development (AID) and the Government of the Philippines (GOP) completed the design of the three-year Decentralized Shelter and Urban Development program (DSUD) (USAID/Philippines, 1990a). The program will provide \$50 million in Housing Guaranty (HG) loan resources along with \$4 million in Economic Support Fund (ESF) monies for technical assistance and training. To benefit from these resources, the GOP has agreed complete a series of actions specified in a Policy Matrix directed toward the achievement of the program's overall goal:

To foster a greater role for elected city governments, the private sector, and NGOs in the development of shelter-related infrastructure in the chartered cities in order to increase, over an extended period of time, the access of low-income Filipinos to shelter and services needed for healthier and more productive lives.

The Implementation Agreement (signed in May 1991) calls for the disbursement of HG funds in three tranches (of \$20 million, \$15 million, and \$15 million, respectively). The purposes of this report are: (1) to assess the progress made by the GOP on its agenda as a basis for decisions concerning AID's authorization of the first borrowing; and (2) to review factors that may be constraining achievement and suggest ways the program could be strengthened.

DSUD AND BASIS FOR ASSESSMENT

DSUD was designed to directly support selected elements of a broader GOP program to decentralize *authority* to local governments and assist them in developing the *resources* and *capacity* needed to carry out their new responsibilities efficiently and effectively. A number of past AID projects in the Philippines have supported these ends.

Most current AID assistance in this regard is being provided through two companion programs: DSUD and the Local Development Assistance Program (LDAP--see USAID/Philippines, 1990b).

DSUD focuses on: (a) chartered Cities (these include all of the nation's larger urban centers, although particular emphasis is being given to Cities outside of Metropolitan Manila)¹ and (b) improving the delivery of shelter and related infrastructure and services in those cities. In contrast, LDAP concentrates on: (a) local governments responsible for smaller towns and rural areas, and (b) more general administrative and fiscal improvements. DSUD's Policy Matrix specifies contributions to three objectives for the Cities:

1. Develop a self-sustaining system of financing.
2. Improve the delivery of urban services and infrastructure.
3. Improve access to sustainable urban shelter delivery for low-income households.

Under the DSUD agreement, in addition to taking actions to achieve these goals, the GOP must also meet an investment plan requirement: i.e., that 125 percent of the peso equivalent of all HG funds received be invested in shelter related improvements benefitting below-median-income households in the Cities.

The broader GOP decentralization effort includes yet other activities that are not addressed directly by the Policy Matrices of either DSUD or LDAP--most critically at present, the development of a new *Local Government Code* which is to substantially decentralize public sector authority and responsibility and clarify intergovernmental relations.

The assessment of DSUD achievements must first be based on the specific targets set in its own Policy Matrix. However, commentary pertaining to the Implementation Agreement recognizes that the broader decentralization program must also be considered. For example, although DSUD was designed so that it could succeed regardless of the fate of the new *Code*, it cannot help but be influenced by the progress of that agenda as well as other decentralization activities being undertaken by government. If the broader program becomes bogged down, DSUD objectives will be harder to achieve. Alternatively, temporarily slow progress on some element of DSUD would be interpreted more positively if substantial achievement in the broader program promised to motivate better performance in that area in the near future.

¹Whereas much HG related documentation regularly refers to "chartered Cities", this report simply refers to them as the "Cities", since that is the more common term for them in the Philippines (see further definitions in Section 2).

OVERALL CONCLUSIONS

In light of the findings summarized in the paragraphs to follow (and discussed in more detail in the body of this report), the overall conclusions of this assessment are:

1. The GOP has made significant progress on all requirements specified in the DSUD Policy Matrix as the basis for the initial borrowing. Of the ten targets related to the first tranche, eight appear to have been met satisfactorily (although opportunities for further strengthening are pointed out in a few of these areas), and enough progress has been made on the remaining two to suggest they will be achieved shortly. Also, although final certifications have not been provided, preliminary tabulations indicate that sufficient HG-eligible investments have been made to satisfy the investment plan requirement for the first tranche.

2. The overall decentralization program is clearly one of the government's highest priorities. The reconciliation of legislative drafts for the new *Local Government Code* is now in its final stages and passage appears imminent (full implementation is to occur six months after passage). To be sure, there are those who favor slower change than that called for in the current drafts, but the political momentum behind decentralization is substantial. Even if current provisions are watered down or passage is delayed, it seems highly improbable that the basic course toward decentralization will be altered fundamentally.

3. Our assessment of the overall program suggests that there is an urgent need to expand and expedite the technical work needed for the effective implementation of decentralization. More forceful coordination and guideline development at the central level and more aggressive "demand-driven" capacity development at the local level, appear critical at this point (see recommendations below). The rapid and well-focused deployment of DSUD technical assistance and training resources can make an important contribution to these ends.

PROGRESS OF THE PHILIPPINE DECENTRALIZATION PROGRAM

Many observers of Philippine governance argue that the need for the substantial decentralization of public sector functions has existed for decades. However, the urgency of this movement has clearly increased. In the 1970, only 11.7 million people lived in urban areas (32 percent of the national population). In the 1970s, however, urban areas grew by an average of 626,000 per year (55 percent of national population growth). The urban growth increment in the 1980s was 830,000 per year (62 percent) and the GOP estimates urban areas will have to accommodate 1.0 million new inhabitants annually in the 1990s (73 percent). Given the implied acceleration of urban service needs and poverty in the cities and towns, it has become even more clear that this growth cannot be managed effectively from Manila.

Accordingly, the current government has made decentralization one of its highest priorities. In 1988, the President established a Cabinet Action Committee on Decentralization (CACD) and a Pilot Decentralization Project (PDP) which entailed more

aggressive implementation of decentralizing activities already underway (and the development of new Presidential directives to fill gaps) in order to support decentralization as far as possible within the framework of existing law. Substantial new budgetary allocations have also been made directly to several Provinces under the PDP. In 1990, the Cabinet Decentralizing Implementing Team (CDIT) was created to expedite the process. Progress under these efforts has been mixed, in many ways falling short of initial expectations. Nonetheless, the pressure from the President to further the program remains intense.

Work on the legislative front to reform the *Local Government Code* has been active in both houses, culminating in present efforts to reconcile drafts. The Senate bill calls for substantial devolution of authority for many government functions and an increase to 40 percent in the share of centrally raised internal revenues automatically granted back to localities. The increased participation of the private sector and NGOs is stressed. The bill also calls for the secondment of a large number of central government employees to local governments. The House bill implies less dramatic reform in several areas, although even it would represent a marked change from the status quo. At this point, accounts in the press indicate that most of the provisions of the Senate bill are being supported in the conference committee, although serious differences remain on some points.

Although the opinion that a new *Code* will be passed soon appears dominant, it is of course impossible to predict the outcome with certainty. Passage could be delayed. Nonetheless, it appears highly unlikely that movement toward decentralization would be stopped even if that occurred. Pressure from popularly elected Provincial Governors and the Mayors of large Cities (which are accounting for an accelerating share of the electorate) is at a high point. All of the announced candidates for the upcoming presidential election have pledged support for decentralization. (National elections are scheduled for May 1992 and local elections are expected in October 1992).

Another factor to be considered in this assessment is the high priority the AID Mission in the Philippines has itself given to the program. Decentralization is one of the three main themes of its Philippine Assistance Strategy (FY 1991-1995) that cut across all programmatic objectives (the other two being policy reform and the private sector). The Mission has backed up this priority with a highly competent professional staff to directly administer DSUD, LDAP and other AID decentralization focused initiatives and has implemented internal processes that reinforce concern for decentralization within other substantive programs.

PROGRESS OF THE DSUD AGENDA

Progress under each of the implementation actions identified to achieve the program's three goals for the Cities is summarized below.

1. Develop a self-sustaining system of financing

a. Improved tax collection. No target was set for the first tranche in this area. Nonetheless, efforts to improve collections have continued. Preliminary Department of Finance data indicate that, for all chartered Cities from 1989 to 1990, property tax revenue increased from P1.54 billion in 1989 to P1.82 billion (an 18 percent increase), and business tax revenue grew from P1.03 billion to P1.14 billion (an increase of 11 percent).

b. Recommendations to overcome systems constraints. As required, a scope of work has been prepared for a study that will assess constraints preventing the Cities from developing self-sustaining systems of financing and recommend steps to overcome those constraints. While this represents a good start, it will probably have to be further detailed to ensure that constraints are adequately researched and reports contain recommendations that are explained sufficiently to facilitate rapid follow-up activity.

c. City issued bonds and other credit instruments. As required, a scope of work has been prepared for a study to review the current Presidential Decree (P.D. 752) which regulates City use of credit financing and make recommendations on its improvement. Also, the nation's first local government bond issue (for Cebu Province) was successfully floated earlier this year. Plans are now being made for an additional issue for Quezon City.

2. Improve the delivery of urban services and infrastructure

a. Commercial approach to cost recovery. The first tranche milestone in this area was the preparation of a draft guideline for Cities in the planning and implementation of cost recovery for at least one service, most probably, solid waste collection. Delays in the contracting process prevented this milestone from being achieved before this assessment. However, the Department of the Interior and Local Government (DILG) is making considerable progress and the draft should be complete shortly.

b. Private sector delivery of basic services. As required, the DILG issued a guideline (in December 1990) enabling Cities to involve the private sector in delivering services such as solid waste collection, the operation of public markets, and road maintenance. The guideline is general, however, and more detailed manuals will be needed to support implementation.

c. Capital investment programming. As required, the scope of work has been prepared for a project to review the Capital Investment Folio process (a financially disciplined approach to capital budgeting originally developed for Metropolitan Manila) and make recommendations as to how it should be modified for implementation in other Cities.

d. Devolution of responsibilities for public works implementation. The milestone required for this element was the signing of a Memorandum of Agreement

(MOA) between the Department of Public Works and Highways (DPWH) and the League of City Mayors giving Cities authority to implement some local public works projects. At the time of this assessment, negotiations were well along, but the MOA had not been signed. However, there are reasons to expect continued positive movement in this area. Similar MOAs have been signed with the Leagues of Provinces and Municipalities and, actual devolutions of authority have been made to some local governments. The commitment of the DPWH to proceed with this approach has been clearly demonstrated. (Since present drafts of the proposed *Local Government Code would grant this devolution and more for all Cities*, future milestones specified in the Matrix for this element would, of course, have to be reevaluated, and modified appropriately, if the new *Code* is passed in that form).

3. Improve access to sustainable urban shelter delivery for low-income households

a. Use of idle public lands and updating town plans. Technically, both of the targets set under this element have been met. First, the Land Management Bureau (LMB) is continuing an ongoing program to inventory public lands. Second, the Housing and Land Use Regulatory Board (HLURB) has begun a work program, targeting specific Cities for town plan updates. Work in these areas needs strengthening, however. LMB needs support to move from inventorying work per se to give more emphasis to the evaluation of idle lands for reuse or disposition (future DSUD targets in this area may need to be revised to reflect this emphasis). Also a more detailed agenda and schedule for town plan updates is needed. It may be advisable, as an addition to currently specified targets, to require that the future development of urban framework plans be much more closely linked to the process of capital investment programming.

b. Encourage private sector provision of affordable housing. The National Housing Authority (NHA) has developed a program in which it enters into joint venture agreements with private firms to develop sites and services housing for below-median-income families. In this program, the private partner must provide at least 60 percent of the equity. NHA has met target for this element by signing such agreements in six different Cities since the start of 1990. These agreements cover eight projects, that will produce housing for 3,693 households at a total cost of P.331,900; 1,034 of these units had already been completed by the end of March, 1991.

c. NGO/City assistance to associations of informal settlers to acquire and improve homesites. Under the recently launched Community Mortgage Program (CMP), associations of informal settlers can obtain low-rate loans to purchase the land which they are occupying. The community association is held liable for mortgage payments over the first two years. After that, mortgage responsibilities can be transferred to individual households. The initial DSUD target for this element was that the government guarantee payment for at least eight such NGO-assisted schemes in at least four Cities. In fact, during 1990, a total of 51 CMP schemes were initiated in 13 Cities (serving a total 6,866 beneficiary households with a total mortgage value of P.118 million). Also, a cooperative agreement between AID and the Philippine Business for Social Progress (PBSP) is being negotiated under which PBSP will design and carry out a program to strengthen NGO networks and capabilities to further CMP implementation.

The Investment Plan Requirement

The first tranche of HG funds under DSUD is planned at \$20 million. Tabulations of preliminary data by GOP agencies indicate peso expenditures amounting to from \$26.7 million to \$29.7 million in HG-eligible investments during 1990 (from 133 percent to 145 percent of the initial HG tranche), depending on the exchange rate used. Subject to the receipt of certifications from appropriate GOP officials as to the authenticity of these figures, it would appear that the Investment Plan requirement for the first tranche can be met. As will always be the case, some estimates and assumptions lie behind the monetary totals presented. These have been stated explicitly and appear plausible given the data at hand. However, as the Investment Program for the next tranche is being prepared, steps should be taken to check and improve these assumptions and estimating procedures.

CONSTRAINTS AND RECOMMENDATIONS

Even under current laws and regulations, Philippine local governments are not performing all of the functions they have the power to perform, or raising all of the revenue they are entitled to raise. This is partially due to a number of traditional central government practices that reduce their incentives to take charge and, clearly, it is also due their lack of resources and adequate systems and procedures. If a new *Local Government Code* is passed with implementation required in six months, the need to address these constraints in the short term is extremely urgent. No one should expect that they can be overcome in full in such a short period of time. But if substantial improvements are not made very soon, failures in the overall system of government could deter progress toward the nation's fundamental social and economic objectives.

It would appear that the only way sufficient progress is possible, is through a truly cooperative and well coordinated effort on the part of central and local governments--but one in which the primary responsibility for change is placed on the local governments themselves. Experiences throughout the world over the past decade indicate that even well-intentioned efforts by central governments to plan decentralization in detail are doomed to failure. *The job of building effective performance capacity must rest with the localities and the job of central staff must be to facilitate their efforts in that role.*

In discussions with government officials at both levels during this assessment, ideas have emerged that frame several priorities for the process (in general, and in particular as they affect the potential contribution of DSUD).

1. Expedite the development of streamlined implementation guidelines by central government. Once the new *Code* is passed, nothing could threaten its success more than confusion about the way it is to be implemented. There is a need to prepare implementing guidelines and regulations quickly. Most important, those guidelines must be streamlined (clarifying in simple and direct language *what local governments have the responsibility and authority to do and avoiding the temptation to tell them how they must do it*). The DILG has drafted statements of work for developing a conceptual framework for the decentralization process at the central level along these

lines and, in particular, for drafting circulars and guidelines accordingly. This work should be given the highest priority.

However, a key element is missing: the meaningful involvement of local governments in the process of preparing the guidelines. The work statements should be modified to provide for the direct involvement of City officials from the start (e.g. through conferences and local participation in the central coordination process discussed below).

2. Build a more forceful coalition of central agencies to coordinate implementation. Some agency representatives involved in DSUD implementation have recognized the need for more frequent (regularly scheduled) meetings in which: (1) agency representatives review the progress they have made toward stated objectives and discuss the problems and constraints they face; (2) other attendees comment and offer suggestions; and (3) adjustments are made to interim assignments under each objective.

This sort of a process creates pressures for more timely performance. More important, it can build positive and strong interagency ties and comraderie which will be needed during the pressured times that lie ahead. One of the most important opportunities to improve its effectiveness would be to invite representatives from the Leagues of Provinces, Cities, and Municipalities to serve as regular participants.

It would be unreasonable, however, to develop this sort of process for DSUD alone. At the minimum, the process should combine the actions specified under both DSUD and LDAP and become a part of (rather than operate separately from) the overall process that will be established to implement the code (whether managed under a continuation of CDIT or any other entity created for this purpose). It will be important that the participants in this process devote the time needed to follow-through on the details of the agenda; i.e., that it become a true "working coalition". If CDIT itself involves officials at too high a level to play this role, one or more subcommittees may be needed.

3. Develop a "demand driven" system for strengthening local capacities. Strengthening capacities at the local level is the most challenging element of the agenda. In line with international experience supporting the theme above, the approach most likely to fail would be for any central agency to try to plan this process in detail and then enforce local governments participation. The major risks of that approach are: (1) any centrally planned process is unlikely to address the diversity of real local priorities sensitively and will thus waste resources on efforts that do not match true demands; (2) because they do not feel that the capacity strengthening process is "their own", local leaders are certain to criticize it and not take its implementation seriously no matter how well it is designed.

The needs for stronger capacity among the Philippine Cities are uneven. Some City governments are generally stronger, more entrepreneurial, and more effective than others. There are many examples of impressive achievements in recent years by the Cities themselves (e.g., new computer systems, new methods of raising revenue or privatizing services). One promising approach will be to give local officials additional resources for capacity development, encourage them to talk together and share common experiences and problems, and allow them to choose their own priorities and the means of fulfilling them. The most cost-effective means in many cases may be for the officials

of some Cities to copy a success story from one of their other sister Cities. After a Mayor and his or her staff have assessed their own most urgent needs, they are likely to know best how to select services (in some cases choosing a course from a local university, in others using a consulting firm to design and install a new system, in others gaining hands-on assistance from experienced personnel from another City, and in yet others choosing a training course or operational manual developed by a central agency).

This does not mean there is no central role. Central agencies should be active in: (1) evidencing a willingness to serve as cooperative partners in this "bottom up" process; (2) monitoring its progress and providing feedback to suggest opportunities for program enhancement where it is most needed; (3) supporting research and the development of broader monitoring of changing urban conditions (tasks where economies of scale do not permit local implementation); and (4) directly developing some new training courses and operating systems for priority needs depending on their own competitive advantage (recognizing that their products in this regard will have to compete with those offered by other private and public capacity building providers).

One example for consideration is the decentralization program of the Department of the Environment and Natural Resources (DENR) where central government provincial officers play an important role, but they act more as facilitators of the work of their local government counterparts, rather than supervisors.

4. Integrate across DSUD program elements to enhance its contribution to decentralization (particularly with regard to the theme of urban physical development). Considering the objectives of the broader GOP program, it seems reasonable to view the current DSUD Policy Matrix as a starting point rather than a definitive statement of all things DSUD could contribute to decentralization in the Philippines. As the program evolves it may be possible to integrate activity across program elements to enhance accomplishments.

Of course, in light of the approach suggested above, it will be important to gain inputs from City Mayors on comparative priorities before remaining DSUD resources are programmed. Nonetheless, it is possible to illustrate how this sort of enhancement might occur consistent with DSUD themes.

As noted earlier, DSUD's functional specialties are those related to urban services, infrastructure, land, and shelter; i.e. urban physical development. Two key DSUD elements that relate to these specialties are the strengthening of process for budgeting and programming infrastructure improvements (i.e., the Capital Investment Folio approach noted under objective 2c) and the updating of town plans (under objective 3a). Urban master plans have often failed because they have not offered adequate guidance to action programming. Capital budgeting has often run into problems when it has not been guided by some sort of spatial plan for a city that facilitates the geographic coordination of investment; i.e., the capital program can become simply a "collection of projects".

Furthermore, a good spatial framework plan can much simplify the processes of project identification and appraisal. If sufficient economic and cost analysis is provided

to back it up, the plan provides substantial background data and reasoning to support the selection of projects without requiring elaborate and time-consuming appraisals for each project individually; i.e., the program as a whole is appraised in economic terms and individual component projects can be justified with little additional analysis. DSUD resources might help to examine how the town planning and capital programming processes could be linked most effectively in the Philippines.

Similarly, the work on building inventories of public land (objective 3a), the design of innovative but economically viable means of credit financing for infrastructure (objective 1c), the development of approaches to cost recovery and privatization in infrastructure provision (objectives 2a and 2b), and the programming of NHA joint-venture and CMP resources in a city (objectives 3b and 3c) are all closely related to the town and capital investment planning processes. Their contributions should be enhanced if the such relationships between elements are thought through carefully ahead of time.

STRUCTURE OF THE REPORT

The main body of this report backs up the findings and conclusions summarized above. Section 1 examines the context for decentralization in the Philippines, focusing on economic change and patterns of urbanization. Section 2 provides more detail on the progress of the nation's overall decentralization program. The next three sections review in more depth the progress that has been achieved under each of the main objectives of the DSUD policy matrix: improvements to City finances (Section 3), urban services and infrastructure (Section 4), and land and shelter delivery (Section 5). Section 6 presents evidence on GOP progress in meeting the DSUD Investment Plan requirement. Finally, Section 7, examines constraints and offers recommendations for program priorities.

Section 1

**THE PHILIPPINE ECONOMY
AND THE PACE OF URBANIZATION**

The need to decentralize Philippine governance derives from a number of factors. Perhaps the most important is rapid urbanization which, in turn, is largely explained by changes in the structure of the national economy. There are good reasons to believe that managing urban growth effectively requires a different level and mix of government activity than is required in rural areas, and that this public sector "urban package" is much more likely to break down when central governments attempt to provide it (see Kingsley, 1991). This section reviews basic economic and urban trends.

TRENDS IN THE PHILIPPINE ECONOMY

In 1986 the Philippine economy made a strong recovery from the economic and financial crisis of the latter years of the Marcos regime. At the onset of 1983, the Philippine economy experienced a tremendous flight of financial capital. This loss of a substantial amount of the nation's capital and wealth, coupled with a misdirected development plan, not only badly retarded economic expansion in the early 1980s, but also served to further skew the already uneven income distribution.

The Marcos regime's 1983-87 development plan called for an intensive build-up of the industrial/manufacturing sector--a capital intensive sector--which at the time had to rely on foreign sources of capital and material inputs. The early version of this plan virtually ignored the development of agriculture, a sector of the Philippine economy with the greatest potential for leading economic growth due its abundant natural resources and relatively skilled, low cost labor force.

With these policies, the Philippine economy went into a sharp decline in 1983-84. By 1985, it was officially estimated that two thirds of the Filipinos were living below the nation's poverty line, with over 15 percent of the labor force unemployed while 45 percent were underemployed. Concurrently, the government was in debt for \$26.4 billion; a debt level that was attributed to the previous administrations efforts to borrow foreign funds for the overly ambitious industry-oriented development plan.

The strategy of the newly elected Aquino government was to enhance agricultural productivity, as the basis for self-sustaining economic growth. Further stimulation of the economy was directed at liberalization of trade, imports in particular. Initially this policy, combined with a severe austerity program imposed by the IMF, promoted a period of growth and dampened inflation. Starting in 1986, the Philippine economy experienced a period of growth fueled by expanding exports and increased domestic consumption and investment. Moreover, the high prices of the early 1980s were brought down, increasing the real incomes across the income distribution. Table 1.1 shows the net real increase in GNP over the 1983-89 period.

Table 1.1
GNP and Origin of Gross Domestic Product
The Philippines

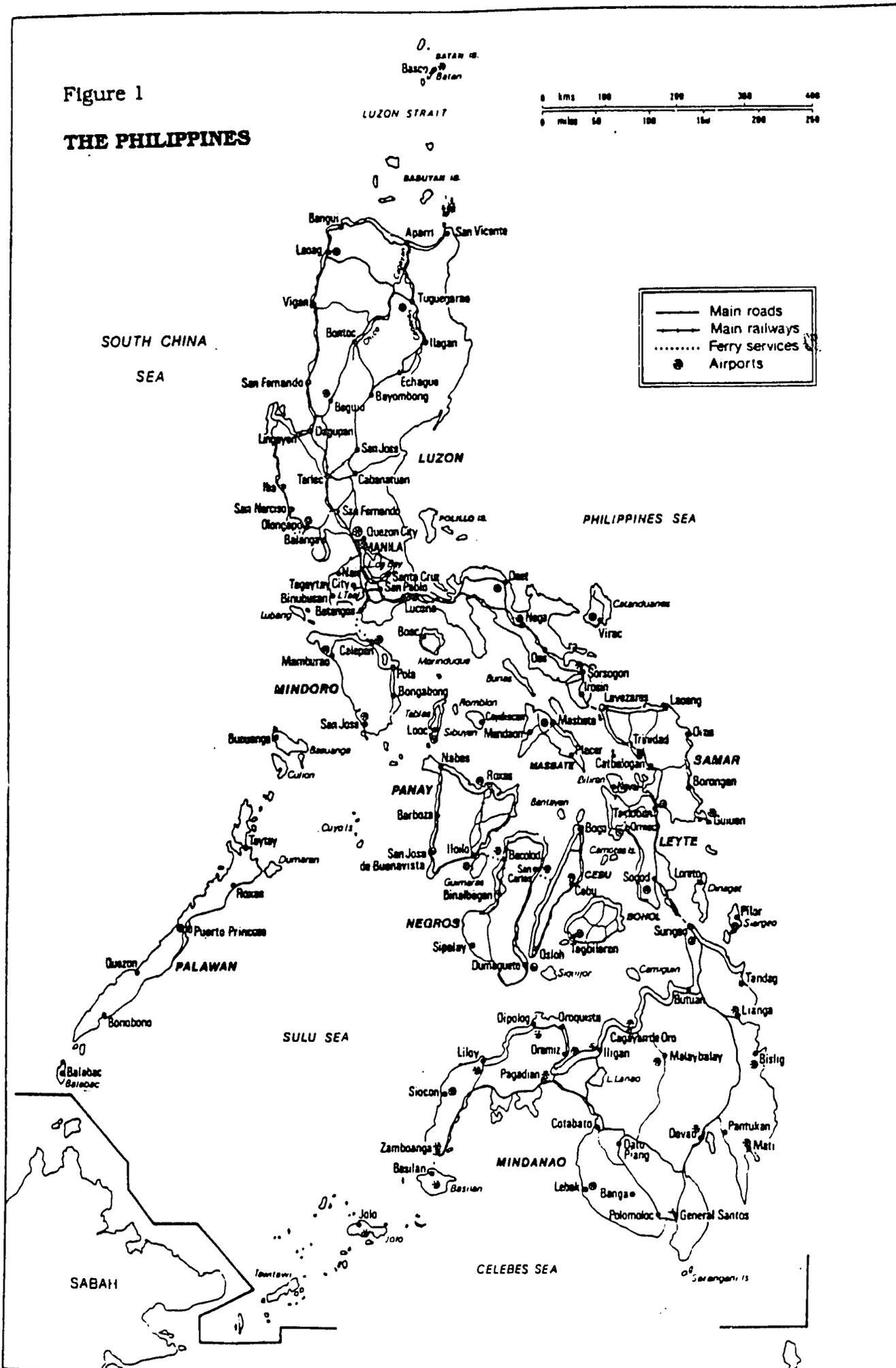
	1983	1984	1985	1986	1987	1988	1989
GNP - Billions of Pesos							
Current Prices	378.8	527.4	597.7	612.0	700.5	816.1	961.4
Constant 1978 Prices	198.8	184.2	169.5	172.3	190.0	203.5	216.8
Pct. Real Increase	1.1	-7.3	-7.9	1.6	10.3	7.1	6.5
Origin of GDP (pct) in constant prices							
Agricul., forestry, fish	24.9	27.1	29.3	29.8	28.4	27.4	27.1
Mining	2.0	1.9	2.0	1.8	1.6	1.6	1.5
Manufacturing	25.1	24.8	23.9	23.8	24.3	24.9	25.1
Construction	7.7	6.3	4.8	3.7	4.2	4.2	4.6
Utilities	1.2	1.4	1.6	1.9	2.0	5.4	2.0
Trans. and communication	5.3	5.3	5.5	5.6	5.5	2.0	5.3
Commerce and finance	21.5	20.4	20.2	15.7	15.8	15.6	15.6
Government and service	12.3	12.8	12.8	17.8	18.3	18.9	18.7
Total	100.0	100.0	100.0	100.0	100.0	100.0	100.0

Source: IMF 1991, NEDA 1990.

Table 1.1 also shows how the sectoral distribution of GNP changed during the recovery period. Manufacturing, utilities, and the service sector all experience notable increases in share between 1985 and 1989. While agriculture's share declined somewhat over this period, it still experienced substantial real growth. Increased exports as well as domestic investment during this time were fueled by the production of coconut oil, the leading export of the Philippines which accounts for over half of the total world production.

Figure 1

THE PHILIPPINES



The Philippine economy weakened again in 1989 as a result of policy slippage and an extraordinary series of adverse shocks. A coup attempt in late 1989 along with a severe drought and a earthquake coupled with a later typhoon in 1990 combined to lower exports and wreak havoc with the local infrastructure. In addition to these unexpected supply shocks, a 40 percent increase in the minimum wage mandated by Congress helped to cost/push prices higher in 1989, and lower the Government's overall projected macroeconomic target of positive real growth.

Even though the expansion of agricultural output was an important story in the Philippine economy in the late 1980s, it did not alter the longer term structural trend in employment (Table 1.2). Nonagricultural employment expanded from 50 percent of all

Table 1.2
Structure of Employment, 1983-1989
The Philippines

Sector:	Percent of Total						
	1983	1984	1985	1986	1987	1988	1989
Agriculture	54.4	49.6	49.0	50.0	47.8	47.7	44.8
Mining and Quarrying	0.5	0.7	0.6	0.7	0.7	0.8	0.8
Manufacturing	9.8	9.8	9.7	9.2	9.9	10.2	10.8
Electricity, Gas and Water	0.4	0.4	0.4	0.3	0.4	0.4	0.4
Construction	3.6	3.9	3.5	3.1	3.6	4.0	4.4
Wholesale and Retail Trade	11.4	12.4	13.2	13.7	13.7	13.2	14.0
Transportation and Communication	4.3	4.5	4.7	4.1	4.5	4.8	4.9
Finance, Insurance and Business Services	1.9	1.9	1.7	1.9	1.9	1.9	1.8
Government, Community and Social	16.6	16.8	17.2	17.1	17.4	16.9	18.1
TOTAL	100.0	100.0	100.0	100.0	100.0	100.0	100.0

Source: NEDA, 1990.

jobs in 1986 to 55 percent in 1990--substantial change in such a short period of time. Actually, this trend is not surprising in a healthy development transition. Agricultural expansion is accompanied by significant improvements in productivity that require fewer workers per unit of output. Agricultural growth creates demand for new and better products from nonagricultural sectors. Nonagricultural jobs offer higher wages (the average non-agricultural wage outside of metropolitan Manila in 1989 was 35 percent higher than the average national agricultural products. As the shift to nonagricultural employment occurs, it inevitably implies a shift in location toward urban areas since the efficiencies of locations in cities and towns are important to the competitiveness of most manufacturing, commercial, and service enterprises.

URBANIZATION AND ITS IMPLICATIONS

Urbanization. Data in Table 1.3 indicate that from 1970 to 1990 the population of Philippine urban areas grew at an annual rate of 4.1 percent, compared to a 2.6 percent growth rate for the nation as a whole. An urban growth rate of 4.1 percent is substantial in world terms (the U.N. estimates that urban areas in all of the world's less developed nations grew at an annual rate of 3.8 percent from 1960 to 1990--United Nations, 1987).²

	Population		Urban Pct.
	Total	Urban	
TOTALS			
1970	36,685	11,678	31.8
1980	48,098	17,944	37.3
1990	61,480	26,246	42.7
2000	75,224	36,263	48.2
GROWTH			
70-80	11,413	6,266	54.9
80-90	13,382	8,302	62.0
90-00	13,744	10,017	72.9
Source: NEDA, 1990.			

GOP forecasts indicate that in the 1990s the urban rate will drop to 3.3 percent, and that the total national rate will drop to 2.0 percent. But this shift does not imply any diminution of the pressure for new infrastructures and services in cities and towns. Though the percentage rate will be lower, the absolute magnitude of urban growth is still increasing. In the 1970s, urban areas grew by an average of 626,000 per year (55 percent of national population growth). The urban growth increment in the 1980s was 830,000 per year (62 percent) and the GOP estimates urban areas will have to accommodate just over 1.0 million new inhabitants annually in the 1990s (73 percent).

²All data on 1990 populations presented in this Section are preliminary census figures. Interpretations presented here would have to be modified if final census data differ in any significant way from the preliminary counts.

The System of Local Governance. At the local level, who is responsible for managing this growth? Responsibility below the central level falls first to 91 governmental units: 16 "Highly Urbanized Cities" and 75 Provinces.³ Province territories are further subdivided into Municipalities (total of 1,531) and, in some Provinces, Component Cities (total of 44). Component Cities have powers and responsibilities exceeding those of the of Municipalities but, unlike the Highly-Urbanized Cities, they still fall under the jurisdiction of the Provincial Governors.

Established standards call for Municipalities to be reclassified as Component Cities when their populations exceed 100,000 and their annual incomes exceed P.10 million, and for Component Cities to be reclassified as Highly-Urbanized Cities when their populations exceed 150,000 and their annual incomes exceed P.30 million. Such reclassifications, however, have occurred before those standards have been reached.

At the lowest level, all national territory is divided into 40,650 Barangays (villages). Based on population density and other factors, Barangays are classified as either urban or rural. Both types can and do exist in all of the intermediate level territories defined above. Even Highly-Urbanized Cities contain rural Barangays, sometimes a large number. Some Municipalities are entirely rural, but many contain urban Barangays. Thus urban growth management responsibilities exist at all local government levels above that of the Barangay.

Importance of the Cities. Table 1.4 shows that the 60 chartered Cities which are the focus of DSUD (14 Highly-Urbanized Cities plus 46 Component Cities) had a total 1990 population of 13 million, about half of the urban total for the nation as a whole. Actually their share of the urban population is somewhat below that since the Cities also contain some rural population (the rural fractions within cities cannot be sorted out until further data from the 1990 census is released). The Cities' average population growth rate over the 1980s was 2.4 percent, but it is very likely that rural populations within the their boundaries declined over the decade and, thus, that their urban growth rate was considerably higher than that.

The table also shows that, much to the relief of many observers, the Cities in the NCR (metropolitan Manila) grew more slowly in the 1980s than those in other regions: an annual rate of 2.0 percent, compared to 3.1 percent for Cities in Mindanao, 2.5 percent for those in the rest of Luzon, and 2.4 percent for those in the Visayas.

³For a number of purposes, the Provinces and Cities are grouped into 13 regions, one of which is metropolitan Manila, or more formally, the National Capital Region (NCR). A number of governmental functions are performed at the regional level through bodies such as the Regional Development Councils (made up of Province Governors and City Mayors) and Regional Assemblies (made up of Congressmen), but these functions are basically coordinative. With two exceptions, there are no general purpose governments with independent executives and legislatures between the central level and the level of the Provinces and Highly-Urbanized Cities. The exceptions are the NCR and the autonomous regions. A full description of the system of local governance in the Philippines, and the history of its evolution, is found in Ocampo and Panganiban, 1985.

Table 1.4
POPULATION GROWTH ANALYSIS: THE NATION AND THE CITIES

	Total	Nat. Cap. Region	Other Luzon	Visayas	Mindanao
TOTAL PHILIPPINES					
Population (000)					
1970	36,682	3,967	15,720	9,031	7,964
1980	48,098	5,926	20,155	11,112	10,905
1990	60,479	7,832	25,404	13,020	14,223
Annual % Growth					
1970-80	2.7	4.1	2.5	2.1	3.2
1980-90	2.2	2.8	2.3	1.6	2.7
CHARTERED CITIES					
No. of Cities	60	4	20	20	16
Population (000)					
1970	7,442	2,565	1,479	1,846	1,552
1980	10,190	3,552	1,865	2,443	2,330
1990	12,970	4,319	2,385	3,092	3,174
Annual Growth (Pct.)					
1970-80	3.2	3.3	2.3	2.8	4.1
1980-90	2.4	2.0	2.5	2.4	3.1
Annual Growth (000)					
1970-80	275	99	39	60	78
1980-90	278	77	52	65	84

Source: NEDA, 1990.

Table 1.5 shows populations and growth rates for the Cities individually (ranked by size within region). The large and medium-sized cities generally grew more rapidly than the smaller ones, but this correlation is fairly weak and there are many exceptions. In fact, the very largest urban agglomerations (populations over 0.5 million) did not grow as rapidly as those in the middle range. Also, a number of cities with populations above 100,000 grew more slowly than the average for their region (e.g., Angeles, Olongapo, Cabanatuan, Cebu, Cadiz, Calbayog, Zamboanga--the population of Manila itself actually declined over the decade, at an annual rate of 0.3 percent) and a some smaller Cities grew at a pace much faster than the regional average (e.g., Puerto Princesa, Tagaytay, Marawi).

Table 1.5
POPULATION GROWTH ANALYSIS: INDIVIDUAL CITIES

	Population (000)			Annual % Growth	
	1970	1980	1990	70-80	80-90
NATIONAL CAPITAL REGION					
Manila	1331	1630	1587	2.0	-0.3
Quezon	754	1166	1632	4.5	3.4
Caloocan	274	468	746	5.5	4.8
Pasay	206	288	354	3.4	2.1
Total Cities	2565	3552	4319	3.3	2.0
Other	1402	2374	3513	5.4	4.0
Total	3967	5926	7832	4.1	2.8
LUZON					
Angeles	135	189	236	3.4	2.2
Olongapo	108	156	192	3.7	2.1
Batangas	109	144	184	2.8	2.5
Baguio	85	119	183	3.4	4.4
Cabanatuan	100	138	173	3.3	2.3
San Pablo	106	132	161	2.2	2.0
Lipa	94	121	160	2.6	2.8
Lucena	77	108	151	3.4	3.4
Dagupan	84	98	122	1.6	2.2
Legaspi	84	100	121	1.8	1.9
Naga	80	91	115	1.3	2.4
Roxas	68	81	103	1.8	2.4
Puerto Princesa	38	60	92	4.7	4.4
Cavite	76	88	92	1.5	0.4
Laoag	62	70	84	1.2	1.8
San Jose	70	64	82	-0.9	2.5
Iriga	77	66	74	-1.5	1.2
Tagaytay	11	16	24	3.8	4.1
Palayan	8	15	20	6.5	2.9
Trece Martires	7	9	16	2.5	5.9
Total Cities	1479	1865	2385	2.3	2.5
Other	14241	18290	23019	2.5	2.3
Total	15720	20155	25404	2.5	2.3
VISAYAS					
Cebu	347	490	610	3.5	2.2
Mandaue	50	111	180	6.5	5.0
Lapu-Lapu	69	99	146	3.7	4.0
Danao	48	57	73	1.7	2.5
Metro. Cebu	523	757	1009	3.8	2.9
Bacolod	187	262	364	3.4	3.3
Iloilo	210	245	311	1.6	2.46

Table 1.5 (Continued)
POPULATION GROWTH ANALYSIS: INDIVIDUAL CITIES

	Population (000)			Annual % Growth	
	1970	1980	1990	70-80	80-90
Cadiz	100	138	173	3.3	2.3
Tacloban	77	103	138	3.0	3.0
Ormoc	85	105	129	2.1	2.1
San Carlos	84	101	124	1.9	2.1
Bago	72	100	124	3.3	2.2
Toledo	68	92	120	3.1	2.7
Calbayog	94	107	113	1.3	0.5
San Carlos	90	92	106	0.2	1.4
Silay	69	111	92	4.9	-1.9
Dumaguete	52	63	80	1.9	2.4
Bals	40	49	60	2.1	2.0
La Carlotta	38	46	56	1.9	2.0
Tagbilaran	33	43	56	2.7	2.7
Canlaon	24	29	37	1.9	2.5
Total Cities	1846	2443	3092	2.8	2.4
Other	7185	8669	9928	1.9	1.4
Total	9031	11112	13020	2.1	1.6
MINDANAO					
Davao	392	610	850	4.5	3.4
Zamboanga	200	344	444	5.6	2.6
Cagayan de Oro	128	227	340	5.9	4.1
General Santos	86	149	250	5.6	5.3
Butuan	131	172	228	2.8	2.9
Iligan	104	167	227	4.8	3.1
Cotabato	61	84	127	3.3	4.2
Pagadian	58	81	107	3.4	2.8
Surigao	51	80	100	4.6	2.3
Marawi	56	54	92	-0.4	5.5
Ozamis	65	78	92	1.8	1.7
Gingoog	66	80	82	1.9	0.2
Dipolog	46	62	80	3.0	2.6
Dapitan	38	55	59	3.8	0.7
Oroquieta	39	47	53	1.9	1.2
Tangub	31	40	43	2.6	0.7
Total Cities	1552	2330	3174	4.1	3.1
Other	6412	8575	11049	2.9	2.6
Total	7964	10905	14223	3.2	2.7
TOTAL PHILIPPINES					
Total Cities	7442	10190	12970	3.2	2.4
Other	29240	37908	47509	2.6	2.3
Total	36682	48098	60479	2.7	2.3

Source: NEDA, 1990.

Section 2

**GOVERNANCE AND
DECENTRALIZATION**

Decentralization and local autonomy are not unfamiliar terms in the Philippines. Serious efforts to promote them have been made several times since the end of Spanish colonial rule in the late 19th century (see Ocampo and Panganiban, 1985). But to this point, none has substantially diminished the central government's control over public sector activities in local areas.

Nonetheless, political pressure for decentralization has intensified over the past few years, now apparently reaching a crescendo. The main purpose of this Section is to describe what the executive and legislative branches of the GOP have done to respond to this pressure. As background, however, we open with brief descriptions of the central government's role in local development, and the powers of Local Government Units (LGUs), at present.

THE CENTRAL ROLE

The central government is composed of three basic institutions: the Presidency, the legislature (Batasang Pambasa), and the courts. The two houses of the legislature are the Senate (with Senators, elected at large nationally) and the House of Representatives (with Congressmen elected by the constituents of separate districts).

Under the direction of the President, the executive branch is made up of a sizeable number of Ministries (Departments) and special agencies. Each Department is headed by a Minister, appointed from the elected members of the House. Public functions are also carried out by a variety of government owned corporations, established to fulfill special functions.

The Departments and corporations most actively involved in local development are noted below (all have responsibilities under DSUD). The first four are responsible for central oversight of local governments.

- o *The National Economic and Development Authority (NEDA)* formulates national economic and investment policies and plans and coordinated public sector development activities.
- o *The Department of Finance (DOF)* oversees the distribution of central government grants and the financial management and revenue activities of LGUs.
- o *The Commission on Audit (COA)* audits financial reports by all levels of government.
- o *The Department of the Interior and Local Government (DILG)* is responsible for the police function nationally and is the main link between the central government and the LGUs: dealing with questions regarding their jurisdiction and status, regulating their activity, and monitoring and supervising their performance.

The following central agencies are responsible for shelter and infrastructure services in localities.

- o *The Department of Public Works and Highways (DPWH)* builds most of the infrastructure in the nation (roads, drainage improvements, sanitation systems, water supply).
- o *The National Power Corporation (NPOCOR)* generates electricity which is distributed through the grids of *The National Electrification Administration (NEA)*. (It is then sold to local and electrical utilities for distribution to consumers).
- o *The Land Management Bureau (LMB) of the Department of the Environment and Natural Resources (DENR)* is responsible for inventoring and managing nationally owned public lands.
- o *The Bureau of Lands (BL)* within the *Department of Justice (DOJ)* is responsible for regulating private land registration and transfer.
- o *The Housing and Urban Development Coordinating Council (HUDCC)*, under the Office of the President, coordinates housing policy and the activities of the following agencies.

- o *The National Housing Authority (NHA)* is responsible for direct government housing production programs for low-income households (although it is now shifting emphasis toward joint-venture production with private developers).
- o *The National Housing Mortgage Finance Corporation (NHMFC)* provides long-term mortgage financing for home purchases.
- o *The Housing Insurance and Guaranty Corporation (HIGC)* provides various housing guarantee and loan insurance related to housing.
- o *The Housing and Land Use Regulatory Board (HLURB)* administers land development regulations and coordinates and supervises local physical planning.

LOCAL GOVERNMENT

The Philippines is a unitary state. The national government thus retains the authority to determine how local governments are created and to define their functions and the processes by which they select their leaders and carry out their responsibilities.

The present functions of each type of LGU (see Section 1) are set forth in the *Local Government Code*, last enacted in 1983 (Batas Pambansa Blg. 337). All units (from the Provinces and Highly Urbanized Cities to the Barangays) have popularly elected executives and councils (Sangguniang Bayan). The list of functions they are legally authorized to perform is quite broad. Higher levels can prepare plans for their own development, levy and collect several types of taxes, establish and operate public markets and other enterprises, provide many services, and regulate private activity within their boundaries.

However, all of these functions are regulated and supervised by central officials. Central Departments have the right to review and either ratify or amend most local programs. Also, as noted above, many services and the bulk of local infrastructure are still provided directly by the central government.

Over the past several years, central Departments have *deconcentrated* considerable authority to their own officers located in the Provinces. Governors and Mayors do not have to deal with Manila as often, but they still have to deal with officials representing Manila. Local executives are able to appoint their own staffs for the most part, but local Treasurers are appointed by, and serve as employees of, the central government.

THE PRESIDENT'S DECENTRALIZATION PROGRAM

Decentralization has been one of the main themes of President Aquino's administration. She has issued a number of memoranda-circulars furthering the deconcentration of central agency functions to regional and local offices but, more to the point, she has been a champion of the true devolution of authority and resources to local governments.

In 1988, she established the Cabinet Action Committee on Decentralization (CACD) and the Pilot Decentralization Project (PDP).⁴ The overall strategy was to : (1) more fully implement existing laws and regulations permitting additional decentralization; (2) find gaps in existing executive pronouncements and issue new Presidential Directives to fill them in order to further decentralization to the extent permitted under existing law; and, then, (3) pursue additional political, administrative, and fiscal reforms and encourage the development and enactment of a new legal framework supporting decentralization (a new *Local Government Code*).

In the first stage of the PDP, the Governors of four Provinces were give a lump sum allocation of P. 120 million each to spend according to priorities determined by their own governments. (Other Provinces were later added to the program, but they were granted much smaller lump sum allocations). Many discussions between central and local officials on means of decentralizing within existing law, and a number of Memoranda of Agreement (MOA) were drafted that would devolve more authority to the local level in the PDP Provinces.

Progress under initial PDP implementation has been mixed. Indeed a number of infrastructure and livelihood projects have been initiated that might otherwise not have been funded. However, there have been questions about how efficiently the funds have been used--charges have been leveled that one Governor, in particular, mishandled the additional PDP resources he received. Also, few of the drafted MOA have actually been signed and true shifts of functional responsibilities appear minimal to date.

The President has taken steps recently to reinvigorate her decentralization initiative. A new Cabinet Decentralization Implementing Team (CDIT) was set up in March 1990 to manage the process more forcefully, and more use is being made of directives from the Office of the President, instructing central agencies to be explicit about their decentralization programs (a new wave of circulars was issued in July 1990, covering an expanded list of agencies). Emphasis is now being given to pilot tests of specific changes and, generally, to more involvement of the private sector and NGOs in service delivery. The number of PDP Provinces has been expanded to 19 in total. The President also continues to work actively in support of passage of the new *Local Government Code*.

⁴This discussion is drawn largely from Yotoko (1991) which reviews both the progress and the problems of the President's program in some depth.

While achievements have not met original expectations, the issues entailed in implementing decentralization are at least being joined in a serious manner. Elected local leaders are clearly appreciative of the President's efforts. Interviews conducted during this assessment uniformly indicated that their frustrations about progress to this point have led to a yet more intense political clamoring for change (rather than any loss of interest or hope). This pressure is now being focused on the process of amending the *Code* in the legislature.

PROGRESS IN THE LEGISLATURE

At the time of this assessment, drafts for the new *Local Government Code* had been prepared by both houses and were in the process of reconciliation in conference committee. The following summary is based on recent reviews of status by Dickherber (1991) and Yotoko (1991). Both consider that the provisions of the Senate version are most likely to be passed in most areas so the following describes that draft in the main, noting provisions of the House version only where significant difference still remain.

Devolution of Functions. The draft provides for the devolution of a number of specific function to LGUs. Perhaps the most important concerning urban development is the "construction, improvement, rehabilitation, repair, and maintenance of all infrastructure facilities intended primarily to service the needs of the residents of" the LGU (i.e., this would include local water supply and residential service roads, but not inter-provincial highways). Also important, the LGUs are given the power to authorize the reclassification or conversion of agricultural lands and provide for the manner of their disposition (although there are some limits on the amounts that can be reclassified). Other functions specifically devolved include social welfare services, field and community health services, implementation of low-income housing programs (with some limitations), development of tourism facilities, and extension services related to agriculture and fisheries. The principle of "subsidiarity" is applied to avoid overlaps in responsibilities; i.e., powers specifically devolved in the *Code* are no longer included among the responsibilities of higher levels of government.

Changes in the Operations of National Agencies. Regional and local offices of central agencies whose functions are devolved are to distribute appropriate property and equipment to the LGUs. Also, affected staffs of these offices are to be transferred to LGU payrolls (with the provision that their compensation not be reduced as a result). Such agencies previously responsible for frontline services are hereafter to confine their activity to the formulation of national plans and programs and the setting of standards and guidelines for LGU performance. These agencies are to continue to monitor LGU compliance with these guidelines and standards, but will be able to provide direct technical assistance or supervision only upon order of the President based on findings that the performance of a particular LGU has not been adequate. As a basis for coordination, these agencies are also required to furnish LGU chief executives with copies of reports on their own activities, including budgetary releases.

Local Taxes. The drafts widens local tax bases by giving LGUs access to some taxes previously prohibited for them. It also gives them more flexibility in establishing

tax rates. Whereas the previous *Code* prescribed graduated fixed rates for business taxes (based on gross receipts), the Senate bill leaves rate setting totally up to the local government (the House bill prescribes only a maximum). With respect to property taxes, the proposals empower LGUs to fix assessment levels as a function of the current market value of real property (specifying only maximum levels for different classes of property). Unlike the practice at present, LGUs will retain all property tax revenues collected (i.e., none will be diverted to the national government).

Transfers of Central Revenues to LGUs. At present, LGUs are theoretically entitled to up to 20 percent of national income tax, but recently they have been receiving only about 12 percent. Under the Senate bill, the LGU share would be incrementally increased to 40 percent in 1994 and remain at that level thereafter. In addition, LGUs would be granted 40 percent of the mining taxes, fisheries charges, franchise taxes, and other revenues gained from the development and use of natural resources within their territories. Provisions also call for the automatic release of these funds to the LGUs (payment frequencies have been slow and uncertain in the past). The House bill calls for an LGU share of 25 percent, but this is 25 percent of gross receipts whereas the Senate's 40 percent pertains to receipts net of set-asides to several special central accounts, so the difference may not be as great as it first appears.

Credit Financing. The drafts would allow LGUs to tap private sector credit sources to finance self-liquidating or income producing projects, subject to certain conditions.

Local Development Councils and NGOs. The proposed code requires that each LGU ensure the preparation of a multi-sectoral development plan by its Local Development Council and review and approval of that plan by its *sanggunian*. LGUs will also be obligated to promote the establishment of NGOs within their territories, and permitted to place NGO representatives on their Development Councils and enter into joint-ventures and other collaborative relationships with NGOs.

Section 3

**LOCAL GOVERNMENT
FINANCE**

This Section first summarizes the structure of local government finance in the Philippines and size and compositional trends over the past decade. It then reviews GOP progress and future performance requirements under the first objective of the DSUD agenda: developing a self-sustaining system of local government finance.

THE PRESENT SYSTEM OF INTERGOVERNMENTAL FINANCE

Central Government Expenditures. Table 3.1 shows the changes that have taken place in the Government of the Philippines (GOP) budget in 1986 through 1990 period. On the expenditure side, the most notable highlight during the five years reveals that the GOP's outlays have risen dramatically in the later half of the decade. In 1986 total real government outlays were approximately P31.1 billion and in just five years they increased by more than one third in real terms to P44. billion (constant 1978 pesos). A phenomenal growth rate in expenditures by industrial country standards, and even impressive given the relatively moderate to high inflation rates over the period.

The greatest net increase in GOP expenditures is attributed to a dramatic rise in interest payments on the national debt, which increased from P6.08 billion in 1986 to P14.44 billion in 1990. Alternatively, the fastest falling real expenditure is equity contributions to government corporations, which fell from P4.70 billion in 1986 to just P1.19 billion pesos in a one year period. Thereafter, equity contributions continued to decrease when valued in real and nominal pesos. This dramatic decrease is attributed to the concerted effort on the part of the GOP to lower contributions made to government corporations in the form of equity transfers.⁵

⁵ The government, in the late eighties, launched a massive effort to sell off most of its nationalized corporations in an attempt to further privatize the delivery of services. This effort has obviously been somewhat successful.

Table 3.1
NATIONAL GOVERNMENT EXPENDITURES, 1986-1990
THE PHILIPPINES

	1986	1987	1988	1989	1990
EXPENDITURES (constant 1978 pesos, Billions)					
Wages and Salaries	7.04	8.81	10.07	11.59	12.69
Maintenance and Operating Expenditures	4.22	5.13	5.06	6.04	6.12
Interest Payments	6.08	10.04	11.25	12.33	14.44
Subsidies	.48	.65	.77	1.47	1.94
Infrastructure Investment	2.20	1.98	2.14	2.95	2.71
Other Capital Outlays	1.10	1.84	1.67	1.85	3.43
Equity Contributions	4.70	1.19	.45	.50	.59
Loans Less Repayments	4.28	2.06	1.42	.99	1.02
Subtotal	30.42	32.11	33.19	38.17	43.46
Transfers to Local Governments	1.01	1.17	1.07	1.17	1.53
TOTAL	31.10	32.87	33.92	38.90	44.46
PERCENT OF TOTAL EXPENDITURES					
Central Uses	96.78	96.50	96.87	97.02	96.60
Transfers to Local Governments	3.22	3.50	3.13	2.98	3.40
TOTAL	100.00	100.00	100.00	100.00	100.00
PERCENT OF GNP					
Central Uses	17.47	16.60	16.20	17.20	18.96
Transfers to Local Governments	0.59	0.60	0.60	0.50	0.60
TOTAL	18.06	17.20	16.80	17.70	19.56

Source: IMF 1991

The economic crisis of the early 1980s, along with a reduction in public outlays on capital goods and basic maintenance exacerbated the relatively poor condition of the infrastructure. GOP funding for public expenditure on infrastructure actually dropped from 1986 to 1987, and only picked up in 1989 due to a series of natural calamities

striking the island group. Infrastructure investment as a share of GNP in 1986 was 1.3 percent and fell to 1.1 percent of total output in 1988.

Central Government Transfers to Local Governments. The central government transfers a relatively small share of its total expenditure to the Local Government Units (LGUs). Table 3.1 shows transfers to local governments, mainly in the form of Internal Revenue Allotments (IRA), have not increased dramatically during the more prosperous years of the later half of the decade. Transfers grew in real terms from P1.01 billion in 1986 to P1.17 billion in 1989 and further increased to P1.50 billion in 1990. As a percent of total expenditures, the transfers of funds to local governments remained relatively constant from 1986 on, declining slightly in 1989. Though transfers did increase from 1986 to 1990, they remained almost a constant percentage of GNP over the same period.

When compared to selected Asian developing countries, the Philippine's central to local government transfers as a percent of total expenditures is small. The country's transfers to LGUs stood at 2.13 percent of total central government expenditures in 1988, compared to 2.8 percent in Thailand, 5.3 percent in Malaysia, and 17.2 percent in India in the same year (IMF 1991).

Local Government Finance Data. Reliable data for city and local government revenue are available annually by specific category and funding source. Tables 3.2 and 3.3 show real revenue (1978 Pesos, deflated by the CPI) by category for the 1983 through 1989 period as well as revenue as a share of GNP for the same years. Local revenues for Cities are collected mainly through taxation. Taxes are further disaggregated in two distinct categories; (1) the business tax and, (2) the Real Property Tax (RPT). Similarly, non-tax local revenues are also comprised of two categories; (1) receipts from economic enterprises, and (2) user fees. Revenue from the central government is mainly garnered in the form of the IRA.

The Real Property Tax. The RPT in the Philippines is locally administered, though the central government maintains a high degree of control in setting policy over the allocation and collection of property taxes.⁶ In order to mitigate political pressure, the assessors office comes under the jurisdiction of the local civic body though its staff is recruited, promoted and disciplined by the Department of Finance. Tax rates are also set by the central government. Discovery of property is partially based on owner declaration of both urban and rural land and affixed property. The Tax Code (PD 464) assigns assessments ratios to properties that range from 15 to 80 percent, and distributes property taxes by applying nominal tax rates (2 percent in the cities) to the assessed value. Under the current Tax Code, properties are to be revalued every three

⁶ Dillinger (1988) discusses the variation in the different institutional arrangements developing countries institute for property taxes. In doing so, he has defined four categories of property taxation and places the Philippines in the central policy, local administration category.

Table 3.2
CONSOLIDATED REVENUE FOR LOCAL GOVERNMENT UNITS, 1983-1989
THE PHILIPPINES

	1983	1984	1985	1986	1987	1988	1989
REVENUES (constant 1978 pesos, Millions)							
LOCAL:							
Revenue from Taxation	1,150	879	777	868	997	1,033	1,235
Business Taxes	500	383	341	356	350	368	406
Real Property Taxes	650	496	436	510	647	666	829
Non-tax Revenue	920	650	552	614	651	642	905
Receipts from							
Econ. Enterprises	296	228	206	n/a	n/a	n/a	n/a
Fees, Charges and							
Other Receipts	624	422	347	n/a	n/a	n/a	n/a
Subtotal	2,070	1,529	1,330	1,480	1,649	1,675	2,140
CENTRAL:							
Internal Revenue and							
Specific Allotments	1,322	962	885	909	852	991	979
National Aids	192	141	122	124	123	128	141
Subtotal	1,514	1,103	1,007	1,033	975	1,119	1,120
TOTAL	3,584	2,632	2,337	2,513	2,624	2,816	3,261
PERCENT OF TOTAL REVENUES							
LOCAL:							
Business Taxes	14	15	15	14	13	13	12
Real Property Taxes	18	19	19	20	25	24	25
Non-tax Revenue	26	25	24	24	25	23	28
Subtotal	58	58	57	59	63	59	66
CENTRAL	42	42	43	41	37	40	34
TOTAL	100						
PERCENT OF GNP							
LOCAL:							
Business Taxes	0.13	0.21	0.20	0.21	0.18	0.18	0.20
Real Property Taxes	0.18	0.27	0.26	0.30	0.34	0.33	0.40
Non-tax Revenue	0.24	0.35	0.33	0.36	0.34	0.32	0.43
Subtotal	0.55	0.83	0.78	0.86	0.87	0.82	1.03
CENTRAL	0.42	0.60	0.59	0.60	0.51	0.55	0.54
TOTAL	0.95	1.43	1.38	1.46	1.38	1.38	1.57

Source: COA 1983-1986, IMF 1991

Table 3.3
CONSOLIDATED REVENUE FOR CHARTERED CITIES, 1983-1989
THE PHILIPPINES

	1983	1984	1985	1986	1987	1988	1989
REVENUES (constant 1978 pesos, Millions)							
LOCAL:							
Revenue from Taxation	553	378	340	376	364	385	414
Business Taxes	190	135	124	129	131	141	160
Real Property Taxes	360	243	216	247	233	243	254
Non-tax Revenue	290	248	227	211	231	230	270
Receipts from							
Econ. Enterprises	86	76	45	63	44	71	75
Fees, Charges and							
Other Receipts	204	171	182	148	187	159	195
Subtotal	840	626	567	587	595	615	684
CENTRAL:							
Internal Revenue and							
Specific Allotments	473	333	324	283	266	319	348
National Aids	23	14	18	23	24	59	69
Borrowing	29	33	13	9	.8	6	5
Subtotal	525	380	355	315	291	385	422
TOTAL	1,365	1,006	922	902	886.8	1,000	1,106
PERCENT OF TOTAL REVENUES							
LOCAL:							
Business Taxes	14	13	13	14	15	14	14
Real Property Taxes	26	24	23	27	26	24	23
Non-tax Revenue	21	25	25	23	26	23	24
Subtotal	62	62	62	65	67	62	62
CENTRAL	38	38	38	35	33	38	38
TOTAL	100	100	100	100	100	100	100
PERCENT OF GNP							
LOCAL:							
Business Taxes	0.10	0.07	0.07	0.08	0.07	0.07	0.08
Real Property Taxes	0.18	0.13	0.13	0.14	0.12	0.12	0.12
Non-tax Revenue	0.15	0.13	0.13	0.12	0.12	0.11	0.13
Subtotal	0.42	0.34	0.33	0.34	0.31	0.30	0.33
CENTRAL	0.26	0.21	0.21	0.18	0.15	0.19	0.20
TOTAL	0.69	0.55	0.54	0.52	0.47	0.49	0.53

Source: COA, 1983-1989

years based on the current "market" conditions which are determined by the assessors office in concert with area real estate agents.⁷

Business Taxes. The second tax source of revenue for cities is the business tax. In its current form the Local Government Code distributes business taxes according to the type of local government. Thus, the provinces collect taxes on specific industries or services, e.g. printing shops and truck deliveries. While the municipalities are responsible for collecting taxes only on businesses which manufacture or distribute goods. Cities, under the existing code, collect taxes on both provincial and municipal designated types of businesses.

Receipts from Economic Enterprises and Fees. In addition to taxes, Cities collect user fees from operating economic enterprises such as public markets or slaughterhouses. Similarly, statutory user fees are charged for public goods and licenses such as residence taxes, capital revenue imposts, and other user charges. Fees structures for these two categories are usually altered by legislative action only and more often lies at the discretion of the central government.

Central Transfers. The second major component of City revenue is transfers from the central government, predominately the Internal Revenue Allotment (IRA). As noted in Section 2, the IRA is an automatic transfer of the GOP's income tax receipts to LGUs. In its current form, the IRA is based on a formula that allocates funds according to: population (70 percent), land area (20 percent), and equal sharing among LGUs (10 percent). The allocation of the IRA is nonetheless uneven. As city size increases, the proportion of the IRA to total revenue decreases and alternatively, the IRA's growth rates decrease as City size increases (Yotoko 1991). Cities account for approximately 33 percent of total IRA monies distributed to LGUs by the central government. Other central transfers include aids or grants coming from non-government sources usually targeted for a specific purpose (e.g. disaster relief).

Borrowing. The last source of City revenue is borrowing. As shown in Table 3.2 only, borrowing has accounted for a negligible share of total revenue to date. So far, Cities have borrowed for specific capital projects usually related to localized natural calamities. Lenders have been central government corporations or agencies.⁸

Revenue Trends. Tables 3.2 and 3.3 show the real (1978) peso revenue trends over a seven year period, from 1983 to 1989, for all LGUs and Cities respectively. These same tables also show selected revenue categories as a percent of total revenue, and to

⁷ Dillinger (1988) provides a excellent description of the Real Property Tax Administration Project (RPTA) conducted in the Philippines during the early eighties. This ambitious project intended to alter the way property was valued in the Philippines by implementing procedures to better inventory properties through government inspections rather owner-declarations. The program was successful in so far as instituting a better system of valuation, though its impact on collection efficiency was negligible. To date, property revaluation is frequently hotly contested and often postponed.

⁸ As the premier City lender, the NHA total loan portfolio with the Cities is P111 million while, the DILG ranks second with P23 million in outstanding loans.

control for total national output, revenue as a percent of GNP. Furthermore, distinctions in the Tables are made between local and central government sources.

During the 1980s revenue for LGUs and Cities were mainly derived from local sources (approximately 60 percent average annual share).⁹ The rank order by revenue category places the IRA as the foremost contributor to income for Cities as well as LGUs, the RPT is second, closely followed by Fees, charges and other receipts and Business taxes.

Real Property Tax Trends. Tables 3.2 and 3.3 show that revenue from real property taxes contributed about 40 percent of all locally generated LGU and City revenue (25 percent of total revenue) during the 1980s. For Cities, when measured in constant 1978 pesos, the RPT remained relatively constant through the seven year period. The LGU property tax collection effort in the 1980s was slightly better than the Cities' collection performance. When comparing yearly changes, LGUs increased RPT collections at a 18 percent average annual rate from 1985 to 1989, while Cities only managed to increase RPT rates by 5.5 percent over the same period. To further highlight the disparity, the Cities' 1989 RPT collections increased by 4 percent from the previous year, which compares to the LGU's RPT increase of 25 percent in 1989. Notwithstanding the comparison, RPT collections did increase in real terms from 1986 to 1989 period for all LGUs as well as for Cities.

Country Comparison. Relative to other developing countries the Philippines uses the property tax as a major source of municipal revenue. In 1985, the Philippines' share of property tax to total municipal revenue was 20 percent. When compared to eleven other similar income countries, only Kenya (with a 36 percent share) relied on the property tax more to contribute to local municipal revenue.¹⁰

Business Tax Trends. Like the RPT, the business tax exhibited a similar trend over the 1983 to 1989 period. Table 3.2 shows business taxes for all LGUs increasing in real terms, albeit at a slower pace than the RPT. This same pattern is repeated for the Cities as shown in Table 3.3. As a percent of total revenue the business tax fared worse than the RPT. Business taxes for Cities as well as LGUs held relatively constant when measured against total revenue over the seven year period, reflecting no real increase. This same constant percentage pattern over time applies to the business tax as a percentage of GNP for Cities as well as LGUs.

Internal Revenue Allotment Trend. Though the IRA accounts for over 40 percent of the income for LGUs and just under 40 percent for Cities, the IRA has overall

⁹ This figure for the Cities is weighted by the NCR (lower share) contribution to this distribution. Some of the smaller Component Cities rely more heavily on central government transfers, thus their average local/central distribution is closer to an equal proportion between the two sources.

¹⁰ The data are from Dillinger (1988). Property tax comparisons can viewed along different dimensions such as their administrative arrangements as well as valuation methods. The percentages reported here reflect absolute tax levels relative to total recurrent receipts for municipalities (urban portions of eleven countries) during the early to mid 1980s.

decreased in real terms through the 1980s for Cities as well as LGUs. Beginning in 1985 the IRA decreased by about an average annual rate of 13 percent for Cities and 12 percent for LGUs. Not until 1988 did the IRA contribute more in real terms from the previous years level for both Cities and LGUs as a whole (20 percent increase for Cities and 16 percent for LGUs). And when measured relative to total country output, central monies going to Cities decreased as a share of GNP from 1983 to 1987, and then increased only slightly in 1988. A somewhat dissimilar pattern followed for LGUs. In 1983 central government monies as percent of GNP stood at .42 percent, increasing to .60 percent in 1986. In 1987 the transfers decreased and by the end the decade, they ended up at .54 percent of GNP. Therefore, as measured against total national output, the IRAs contribution towards revenue decreased through most of the 1980s for Cities and increased only slightly for LGUs - reflecting a disproportional balance in the distribution of the IRA between Cities and the other LGUs.

Revenue Highlights. Overall, income for Cities and LGUs has not kept pace with the growth of the Philippine economy. Though individual components of revenue have fared better than others, the combined local and centrally transferred income for Cities and LGUs decreased in real terms during 1980s, with the trend being more pronounced for the Cities than the LGUs. Revenue enhancement for Cities as well as LGUs lies with the RPT for it (combined with the business tax) was the major contributor to income in the 1980s.

In 1988 the GOP acknowledged the real decline in local revenue by instituting a massive campaign to increase local government income. Since property taxes contribute the major share of local revenue, the campaign targeted the RPT collection rate and attempted to increase the local assessors ability to value properties.¹¹ The program was moderately successful, largely accounting for the reversal of the downward trend after 1988.

OBJECTIVE 1a - IMPROVED TAX COLLECTION

As noted above, local government tax collections did increase in real terms in the late 1980s, partly due to the priority given to this objective by the DOF--this was in turn supported by technical assistance provided by AID and other donors. The government's DSUD policy matrix calls for further progress in this area.

Requirements. While no DSUD target was set for the first tranche, the Policy Matrix calls for 1991 chartered City tax collections 32 percent above those of 1989 (as a basis for the second tranche) and 1992 collections 58 percent above the 1989 level.¹²

¹¹ At present, the government is debating on how to value property. Properties are currently valued at market estimates of value based on information gathered by local realtors or comparison to similar properties. The debate centers on whether or not valuation of properties should be income based - valued at the level of income for which the property could be rented for.

¹²Such increases are to be calculated based on changes in nominal values.

Progress. Although there was no target for 1990, collections in that year did continue to expand. According to preliminary data from the DOF, Cities collected P.1.14 billion in business taxes in 1990 (11 percent above the 1989 level) and P.1.82 billion in real property taxes (18 percent above the 1989 level). Total City tax collections grew from P.2.56 billion in 1989 to P.2.96 billion in 1990 (an increase of 16 percent).

Comment. A possible constraint on future DSUD targets in this area is that incentives may be weakened by the passage of the *Local Government Code*. As noted in Section 2, the *Code* calls for substantial increases in transfers of central government revenues to LGUs. Given the administrative effort required, and the political risks, accelerating local taxes may not be given as high a priority as it has in the past.

This outlook is illusory, however, since the Cities will also have markedly increased expenditure obligations consistent with the new functional responsibilities being assigned to them. This conclusion will emerge most forcefully in local capital planning processes which require Cities to identify funding sources when they add up the costs of their proposed capital projects for the year (see discussion of Objective 3c in Section 4). There also will be a need, however, for a continuation of technical assistance support in the types of activities that led to the collection increases of the 1980s (better process management, computerization, improved collection procedures, etc.).

OBJECTIVE 1b - RECOMMENDATIONS TO OVERCOME SYSTEMS CONSTRAINTS

Requirements. Here, the target for the first tranche is the preparation of a scope of work for a study to assess factors constraining the development of a self-sustaining finance system for the Cities. Prior to the second tranche, the Matrix requires the completion of the study and the identification of recommended pilot tests of policies to overcome the constraints. Pilot tests are to be underway prior to the third tranche.

Progress. DILG submitted a draft for the required scope of work to AID on April 24, 1991. This document call for research on three types of constraints: the Cities' capacity to expand revenues through more efficient procedures and management; the Cities' capacity to expand their economies and tax bases; and inadequate support systems for local budgeting and financial management.

The framework for the study appears consistent with DSUD goals for this element. However, it does not specify in much detail the purposes and nature of the subtasks required under each component, the methods of analysis to be employed, the manpower loadings to be devoted to each subtask, and the schedule for the work (due dates for each subtask). This study will be among the most important conducted under DSUD, since it will establish the basis for much of the remaining work directed at improving the Cities' financial systems. Accordingly, it would seem appropriate to expand and detail the scope to assure that the results will meet DSUD objectives in full.

OBJECTIVE 1c - CITY ISSUED BONDS AND OTHER CREDIT INSTRUMENTS

As noted on Table 3.2, borrowing has accounted for only negligible share of the funds raised by Philippine Cities to date. Given accelerating demands for capital expenditures with rapid urban growth, however, there is a growing recognition that many benefits can be gained from increasing this share substantially in the future. The DSUD agenda under this objective focuses eliminating barriers to doing so.

Requirements. Prior to the first tranche, the GOP (DOF) is to have prepared the scope of work for a study that will review relevant laws and regulations affecting Cities ability to access credit financing for urban infrastructure (prominently, Presidential Decree 752) and recommend changes that will facilitate City borrowing. The second tranche milestone calls for: (1) implementing appropriate recommendations from the study that are within the purview of the executive branch; (2) recommending to Congress those which require legislative action; and (3) establishing an education program for the Cities to familiarize them with the benefits and methods of credit financing. Prior to the third tranche, at least one City is to have floated a bond issue and the DOF is to have submitted recommendations to the Monetary Board for at least one additional City bond proposal.

Progress. The required scope of work has been prepared and submitted to AID. It reviews the potential importance of credit financing for infrastructure in Philippine Cities and sets forth objectives for the study which are to: (1) examine structural and functional as well as technical problems of bond/credit financing; (2) define the contextual framework of the whole credit financing system in the country as it affects the success of City borrowing; (3) recommend a systems design and/or mechanism of bonds flotation for the Cities; (4) examine more closely selected strategies worthy of scientific examination; and (5) resolve issues and conflicts in bond/credit financing such as the possible "crowding-out" by LGUs of private capital markets. It then provides a fairly detailed and well structured descriptions of the work to be done and the outputs expected.

Comment. An event that warrants mention here (since it has helped to create a more positive atmosphere for City bonds) is the recent bond flotation by Cebu province. Currently, LGUs are granted the authority to issue bonds in P.D. 752. This requires that LGUs first obtain approval from the Secretary of Finance as well as consultations with the Monetary Board and NEDA before bonds are issued. The limit set for issuing a bond by a local government is equal to one-half of one percent to as much as five percent (PD 1195) of the total assessed value of taxable real property within the LGUs jurisdiction.

Even with this authority, LGU bond flotation is difficult today, given cumbersome regulations and the lack of a well defined bond market (as well as a bond rating system). In this environment, the Cebu bond is noteworthy. Cebu province floated the bond in conjunction with the Ayala Land Development Incorporation in 1991. The initial offering was valued at P300 million and redeemable in shares of the Cebu Properties Ventures Corporation. Cebu province's capital contribution was the Lahug Airport, Fuente Osmena and Gorordo, while Ayala Land contributed P63 million. The interest earning amounted to 16 percent a year, with regional brokerage markets at Manila and Makati

stock exchanges issuing the bonds. All the bonds that were issued in the first offering were sold in a short period of time.

Proceeds of the sale are intended to be used to finance various infrastructure projects of the province, one of the most economically dynamic of all provinces in the Philippines. It is nevertheless vulnerable to natural calamities. One such disaster (a typhoon) struck the Island in September 1990 causing extensive infrastructure damage (NEDA estimated the damage to be about P958 million). Demand for capital financing for reconstruction motivated this financial partnership between the province and Ayala--a well established real estate corporation. The primary purpose of the collaboration was to give the bond issue strong financial credibility.

Section 4

**URBAN SERVICES AND
INFRASTRUCTURE**

Structural adjustment programs of the early 1980s often resulted in a cut-back in government investment in local infrastructure. In the latter part of the decade, however, there was a growing recognition of the importance of basic infrastructure to national economic development as well as to addressing social needs and the atmosphere for additional investment has been more positive. Yet it is also being recognized that, in developing countries generally, infrastructure planning, financing, and delivery must be more efficient than it has been in the past. Principles advocated today include: employing affordable technologies and standards, implementing more efficient processes for programming and budgeting investment in line with realistic resource potentials, implementing procedures to recover costs from beneficiaries as far as possible, encouraging greater private sector participation in infrastructure delivery, giving more emphasis to system maintenance, and generally decentralizing responsibility for systems development and operation. (See discussions of these issues in Bahl, 1989, Peterson, Kingsley and Telgarsky, 1990 and 1991b, Rondinelli, 1990).

By a number of its actions, the GOP has generally endorsed these principles (see, for example, Nuqui, 1991). Several have been imbedded under the third objective of its DSUD program: cost recovery, privatization, improved capital budgeting, and decentralization of responsibility. This Section reviews the requirements and progress under each element of this component of the Policy Matrix.

OBJECTIVE 2a--COMMERCIAL APPROACH TO COST RECOVERY

Requirements. Prior to the first tranche under this objective, the GOP agreed to have DILG develop guidelines for Cities to use in planning and operating the cost-recovering delivery of at least one service (e.g., solid waste collection). Before the second tranche, such guidelines are to be developed for two additional services and one or more of these guidelines are to be in the process of implementation in at least three Cities (other candidate services pointed out in the Matrix are transport terminals, markets and slaughterhouses). Prior to the third tranche, implementation is to be underway under such guidelines in a cumulative total of at least six Cities.

Progress. This is one of the two first tranche requirements that had not been completed by the time of this assessment. DILG and AID agreed in early 1991 that consultant assistance to draft the guidelines would be funded out of DSUD technical assistance resources. Due to delays in the contracting process, it was not possible for the consultant to complete the work in time. Discussions with the consultant during the assessment, however, indicated that a sensible work plan was being followed and that the substantive approach being taken should address the issues realistically. At the end of the assessment period, DILG said that the draft guidelines would be complete in two additional weeks. From our observations of the work in progress, we also judge that this work could be completed in that period.

Comment. Once the guidelines are complete and approved within DILG, considerable work must be done to reach the stage where they are being implemented in a significant number of Cities. The guidelines first have to be promulgated. The greatest challenge will then be to encourage Cities to implement them.

The guidelines are expected to be brief and "enabling" in nature, and they should be. But there is a tremendous amount of additional work required; e.g., the development of illustrative case studies, promotional materials, how-to-do-it manuals, and training programs. One of the most important themes in our recommendations (see Section 7), endorsed by a number of central as well as local officials during this assessment, is that the central government cannot orchestrate and control all of this work. The process should be one in which the primary responsibility for change is placed on the Cities themselves and facilitated through their own associations, most importantly the League of City Mayors.

OBJECTIVE 2b--PRIVATE SECTOR DELIVERY OF BASIC SERVICES

Requirements. The first tranche milestone in this area was for DILG to issue policy and implementation guidelines for testing private sector delivery of basic services such as solid waste collection, markets, and road maintenance in the Cities. Prior to the second tranche, at least three Cities are to have issued specific guidelines for service privatization and the private sector should be delivering one or more services in at least two Cities. The third tranche requirement is that the private sector be delivering one or more services in a cumulative total of at least six Cities.

Progress. DILG issued the guideline required for the first tranche (Memorandum Circular 90-104 of December 8, 1990) enabling Cities to involve the private sector in delivering various public services. The guideline is brief, but covers the essentials with sections on: (1) rationale; (2) statement of the objective; (3) operational definition of terms; (4) policies (related to efficiency of service delivery, democratic consultations, transparency of transactions, training and re-training, and overall concern for the public welfare); (5) mode (emphasizing the use of legal contracts); (6) scope (listing of services that can be privatized and roles that can be played by private entities in their delivery); (7) role of the LGUs (e.g., in monitoring and controlling the process); and (8) implementation (requests to work with Local Development Councils and the role of DILG). (Under this guideline, the DILG Regional Directors and field officers are to work with local executives to prepare implementation plans--this role for DILG staff would no doubt be reduced after passage of the new *Code*.)

Comment. Although this guideline has been promulgated, the more complete developmental work needed for widespread adoption and implementation by Cities (similar to that discussed under Objective 2a above) is not far along. Again, discussion in Section 7 about how to mobilize the Cities to do much of this work for themselves is relevant.

OBJECTIVE 2c--CAPITAL INVESTMENT PROGRAMMING

Requirements. In the early 1980s, the *Capital Investment Folio (CIF)* process was designed as a disciplined approach to prioritizing public sector capital projects in Metro-Manila. The process was never fully implemented but it still serves as a model for emulation in Philippine Cities as well as in other countries. Under this objective DILG was to have prepared, prior to the first tranche, a scope of work for reviewing the CIF along with promising capital programming processes from other countries, as a basis for developing better procedures for all Philippine Cities. Second tranche milestones call for the completion of this study (including the development of recommendations and a model capital programming process) and actually developing procedures, providing training, and then trying out the model in at least two Cities. Prior to the third tranche, a cumulative total of at least six Cities are to be trying out the model process.

Progress. The required the scope of work for a project to review capital programming options and recommend a model approach was prepared by DILG and submitted to AID on April 24, 1991. This document reviews the background and rationale for the study, specifies in some detail the methods by which alternative capital programming methods are to be selected for review and compared, and sets forth other requirements of the contractor (including conducting a series of workshops as well as preparing three reports). A six month work period is specified along with a 12 person-month level of effort.

Comment. This may be one of the most critical objectives in the DSUD agenda because how and whether it achieves will say much about the ultimate success of the entire decentralization process. Some additional background information is warranted to provide an understanding of the context.

The Philippines already has a process for preparing capital budgets that is, in many ways, excellent in world terms. Every LGU has a *Local Development Council* that plays a central role in the capital programming process and incorporates a broad range of community leaders in addition to government officials. Each year, the Councils review proposed capital projects and form a proposed list. The proposals of the Local Councils are then reviewed and amalgamated into overall proposals by *Regional Development Councils* (similarly a mix of government officials and private leaders) and their proposals are, in turn, reviewed by *Regional Assemblies* (composed of national legislators from the region at hand, who play an important role in this capital programming process but do not serve as general purpose legislatures in their regions--see discussion in Section 1).

But there are two major problems. First, the Local Councils typically do not follow a disciplined programming process which requires, in essence, three basic steps (steps that are the key features of the CIF): (1) create and prioritize a list of infrastructure projects you would like to build; (2) estimate the total funds likely to be available (from all sources of funds) to pay for those projects; and (3) cut back the list until it fits the amount of funding available. The Councils normally get only as far as step 1; i.e., they create a "wish list" and leave it to others at higher levels to pare it down to fit available resources. (See further discussion in USAID/Philippines, 1990a)

Second, the Councils do not have control over the full range of resources to be spent on infrastructure. All Congressmen have access to separate "Countryside Development Funds" which they can allocate to local capital improvements with a great deal of latitude and independence. There is a natural political competition between the Mayors and Governors (who work through the Local Development Councils) and the Congressmen on resource allocation decisions and, at a minimum, the need for much better coordination.

The process of programming infrastructure investments is perhaps the most powerful tool local leaders have in shaping the physical development of their Cities. The way it is structured has important impacts on their broader strategies and approaches for the activities of local government; e.g., those related to such diverse topics as cost-recovery, the general financing of government, and infrastructure maintenance. Further ideas for improvements to local capital programming processes and the way they can be used to integrate other DSUD objectives are provided in Section 7.

OBJECTIVE 2d--DEVOLUTION OF RESPONSIBILITIES FOR PUBLIC WORKS IMPLEMENTATION

Requirements. The first tranche milestone here calls for the DPWH to have signed a Memorandum of Agreement (MOA) with the League of City Mayors giving Cities the authority to implement some public works projects. By the second tranche, DPWH is to have actually delegated authority and funding (e.g., through City-specific MOAs, as far as is permissible under existing law) to implement such projects in at least seven Cities. The third tranche milestone requires an expansion of the cumulative total to at least 19 Cities.

Progress. This is the second of the two first tranche milestones that was not reached by the time of this assessment. DPWH has drafted the MOA, which specifies the types of infrastructure projects to be devolved along with methods and criteria for selecting Cities for devolution. It has also discussed the draft with responsible officers of the League of City Mayors. However, the MOA has not yet been signed.

However, there are reasons to expect continued positive movement in this area. The DPWH has publicly announced its policy to devolve authority in this manner because it is in its own interests to do so--the types of projects being devolved are small local works that place a significant strain on DPWH staff resources and, thereby, reduce its capacity to handle larger (national and regional scale) projects. DPWH has taken the initiative to successfully negotiate similar MOAs with the Leagues of Provincial Governors and Municipal Mayors (executed July 13, 1990), and actual devolutions of authority consistent with these MOAs have been made to some local governments. The commitment of the DPWH to proceed with this approach appears to have been clearly demonstrated.

Comment. The present Draft of the Local Government Code as proposed by the Senate would grant this devolution and more for all Cities at the time of implementation. If it is passed, future milestones specified in the Matrix for this element would, of course, have to be reevaluated, and modified as may be appropriate.

Section 5

SHELTER DELIVERY

The GOP's housing policies have also changed markedly over the past few years (again see discussion in Nuqui, 1991). In general, the approach is to reduce the government's role as a direct producer of housing and convert it more to one of facilitating housing production by the private sector (formal and informal) as well as focusing available subsidies more tightly on the poor--positions very much in line with the United Nations' (1988) *Global Strategy for Shelter to the Year 2000*. Elements of the new approach have been accepted as policy objectives under DSUD. There are three subobjectives: making better use of idle public lands and updating town plans to support low-income housing; encouraging private sector housing production for low-income groups through joint-venture partnerships with government; and assisting informal urban settlers to acquire and improve their homesites through the Community Mortgage Program.

OBJECTIVE 3a - USE OF IDLE PUBLIC LANDS AND UPDATING TOWN PLANS

Requirements. This objective calls for progress in two interrelated fields. The first is the use of idle public lands in the Cities for low-income housing. By the first tranche, the LMB is to have prepared an action plan for inventorying such land. Further targets call for the start of research for the inventory in at least three Cities, (before the second tranche) and completing inventories in at least three cities and starting research for them in at least six others (before the third tranche).

The second is the updating of town plans (incorporating the specification of effective use of land owned by the national government). HUDCC (actually the HLURB working under HUDCC coordination) is to have prepared a work program for updating town plans prior to the first tranche. The second tranche milestone calls for the completion and ratification of new plans in at least six Cities and the third calls for the

ratification of new plans in six additional Cities plus the ratification of zoning ordinances based on the new plans in the first six.

Progress. Technically, both of the first tranche targets set under this element have been met. First, as per the planning document it submitted to AID on May 2, 1991, the Land Management Bureau (LMB) is continuing an ongoing program to inventory public lands. This plan includes March 1991 directives for organizing steering committees to complete the work in each region, along with a national study group to coordinate the effort.

Second, the Housing and Land Use Regulatory Board (HLURB) has begun a work program, targeting specific Cities for town plan updates. Its City selections (submitted to AID on May 5, 1991) were based on analysis of the status and approval dates of land use plans in all Cities. Priorities for updates were given to Cities whose current plans are most out of date. A total of 26 cities are proposed for the first round:

- Region 1: Baguio, Dagupan.
- Region 3: Angeles, Cabanatuan, Olongapo.
- Region 4: Cavite, Lucena, Puerto Princesa, Trece Martires.
- Region 5: Legaspi, Naga.
- Region 6: Bacolod, Iloilo.
- Region 7: Canlaon, Cebu, Dumaguete.
- Region 8: Ormoc, Tacloban.
- Region 9: Pagadian, Zamboanga.
- Region 10: Butuan, Cagayan de Oro.
- Region 11: Davao, General Santos.
- Region 12: Cotobato, Iligan.

Comment. Work in these areas needs strengthening. First, the LMB needs support (including computers) to be able to record the land inventory systematically and make it more accessible for analysis and decision making. Second, the emphasis in the LMB program should probably move from inventorying work per se toward building efficient procedures for evaluating idle lands for reuse or disposition and implementing those decisions. Third, the inventories would be most useful if priorities were given to those Cities where HLURB proposes land use planning updates in the near term. Fourth, while the HLURB proposals for plan updates has so little detail as to method and schedule that it barely qualifies: further detailing is urgently needed if subsequent milestones are to be met.

Finally, it probably makes sense for HLURB (and others, working in concert with the League of City Mayors) to devise a revised approach for City land use planning. The old "master planning" approach has been criticized in the Philippines, as it has in much of the world, because it is not closely linked to action programming and gives too much emphasis to regulatory controls (see for example, Courtney, 1978, and MacNeil, 1984). Other approaches (e.g., streamlined structure plans developed as a part of the capital budgeting process) are available (see Peterson, Kingsley, and Telgarsky, 1990 and further discussion in Section 7). It may be advisable to revise further DSUD targets in this area to reflect this emphasis.

OBJECTIVE 3b - ENCOURAGE PRIVATE SECTOR PROVISION OF AFFORDABLE HOUSING

Requirements. This objective focuses on a program of housing production in the Cities performed by private firms working under joint-venture agreements with NHA. The Matrix calls for the signing of such agreements in six Cities (first tranche), the start of construction on such projects in six Cities (second tranche), and start of construction in a cumulative total of 12 Cities and the completion of 30 percent of the units in first-tranche projects in at least two Cities (third tranche).

Progress. Data submitted by the NHA on May 7, 1991, shows that it has met the target for this element, signing such agreements in six different Cities since the start of 1990. These agreements cover eight projects, that will produce housing for 3,693 households at a total cost of P331,900; work on 1,034 of these units (28 percent) had already been completed by the end of March, 1991. The Cities include: Davao, Quezon City, Naga, Tagbilaran, and Cagayan de Oro.

OBJECTIVE 3c - NGO/CITY ASSISTANCE TO ASSOCIATIONS OF INFORMAL SETTLERS TO ACQUIRE AND IMPROVE HOMESITES

Requirements. This objective calls for continued progress by the GOP under its Community Mortgage Program (CMP). In this program, NHMFC provides low-rate loans to associations of informal settlers enabling them to purchase and improve the land they occupy (the community associations are themselves held liable for mortgage payments first two years, but they can then transfer those obligations to individual households benefitting from the program). NGOs are making an important contribution in helping the residents of informal communities organize themselves to take advantage of the CMP.

The first tranche milestone specifies program initiation (indicated by the provision of guaranty notes of payment to land owners, putting the funds in escrow, or actual payment of funds) in at least eight NGO-assisted CMP projects in at least four Cities. By the second tranche: (a) cumulative initiation is to be expanded to a minimum of 20 such projects in eight Cities; (b) plans for allotting units are to be completed in at least four projects in four Cities; and (c) at least one basic service (such as water or electricity) is to be provided to at least four projects. The third tranche milestone calls for: (a) cumulative totals for initiation to reach at least 50 projects in 10 Cities; (b) completion of plans for allotting units in at least 10 projects in eight Cities; and (c) the provision of at least one basic service to a cumulative total of at least 10 projects.

Progress. CMP has substantially exceeded the first tranche target. As shown in Table 5.1, during 1990, a total of 51 CMP schemes were initiated in 13 Cities (serving a total 6,866 beneficiary households with a total mortgage value of P.118 million). Another activity which supports this objective is the design of a cooperative agreement between AID and the Philippine Business for Social Progress (PBSP) which is expected to be signed shortly. Under this agreement, PBSP will design and carry out a program to strengthen NGO networks and capabilities to further CMP implementation.

**Table 5.1
COMMUNITY MORTGAGE PROGRAM, 1990 TAKE-OUTS**

City	Date	House-holds served	Mortg. (P Mil.)
Angeles	1/90	2,641	36.797
	10/90	68	1.754
Subtotal	2 Proj	2,709	38.551
Cambanatuan	5/90	44	0.521
Subtotal	1 Proj	44	0.521
Quezon City	3/90	130	1.865
	3/90	8	0.177
	3/90	31	0.340
	3/90	77	1.335
	3/90	13	0.198
	5/90	15	0.180
	5/90	17	0.459
	5/90	11	0.162
	5/90	27	0.793
	4/90	38	0.753
	4/90	114	2.319
	2/90	5	0.105
	6/90	13	0.459
	5/90	16	0.380
	12/90	30	1.332
	5/90	30	1.332
	8/90	10	0.300
	8/90	30	0.823
	5/90	55	1.001
Subtotal	5/90	472	14.000
Subtotal	20 Proj	1,142	28.313
Caloocan City	1/90	302	7.270
	8/90	104	1.135
	6/90	140	2.041
	10/90	84	1.793
Subtotal	4 Proj	630	12.238
Pasay City	3/90	50	1.499
	1/90	69	1.613
Subtotal	1 Proj	119	3.112
Manila	5/90	18	0.605
Subtotal	1 Proj	18	0.605

Table 5.1 (Continued)
COMMUNITY MORTGAGE PROGRAM, 1990 TAKEOUTS

City	Date	Households served	Mortg. (P Mil.)
Davao	5/90	216	4.535
	12/90	33	0.850
	8/90	84	0.720
	7/90	200	0.432
	7/90	143	3.272
	7/90	41	0.375
	4/90	135	1.113
	3/90	98	0.745
Subtotal	8 Proj	950	12.042
General Santos	5/90	146	1.609
	3/90	139	1.296
	7/90	63	0.962
	5/90	215	3.814
	4/90	114	3.358
Subtotal	5 Proj	677	11.040
Mandaue City	12/90	59	1.404
Subtotal	1 Proj	59	1.404
Cebu City	12/90	37	0.808
	1/90	86	0.917
	5/90	15	0.382
Subtotal	3 Proj	138	2.017
Tagabilaran City	12/90	86	2.070
Subtotal	1 Proj	86	2.070
Cotabato	5/90	62	1.188
	6/90	84	1.164
Subtotal	2 Proj	146	2.352
Marawi City	3/90	148	
Subtotal	1 Proj	148	3.746
GRAND TOTAL	51 Proj	6,866	118.102

Source: NHMFC, 1990

Section 6

**PROGRESS UNDER THE
INVESTMENT PLAN**

THE INVESTMENT PLAN REQUIREMENT

The Program Agreement between the GOP and the United States of America for DSUD calls for the GOP to prepare and recurrently update an Investment Plan for City shelter or shelter related infrastructure investment. The plan is to consist of a listing of programmed GOP investments, all of which meet four criteria:

1. They must be investments either directly in shelter, or in shelter related infrastructure (e.g., water supply, access roads).
2. They must benefit households whose incomes are below the national median income (the current official estimate of median income in the Philippines is P5,000 per month).
3. They must exclude any funds (loans or grants) provided by external donors.
4. They must be located in chartered Cities.

Prior to any borrowing, the GOP must provide (and certify to be authentic) a record of funds that have been expended on such eligible projects. The DSUD Program Agreement requires that eligible expenditures so documented must equal at least 125 percent of the amount of the proposed borrowing (e.g., eligible expenditures of a minimum of US\$25 million must be certified and accepted by AID prior to a first tranche

of US\$20 million).¹¹ Certifiable expenditures for the first tranche include those made in 1990 or thereafter. Expenditures certifiable for subsequent tranches, naturally, exclude those certified for earlier tranches.

GOP DATA ON INVESTMENTS FOR THE FIRST TRANCHE

Prior to this assessment, submissions on investments to qualify as a basis for the first tranche were received from several agencies. Assessment consultants and AID staff worked with agency personnel during the assessment period to check data sources and assumptions and make corrections where appropriate. Table 6.1 summarizes the results. Table 6.2 presents the totals for each agency City-by-City. At the time of this report, AID has not yet received GOP certification on the authenticity of these investments but this certification is expected shortly.

Base data were derived from individual agency accounting systems. These data have not yet been audited by COA, but it has been recognized that, because the audit process can take one or more years, it is infeasible to wait for audited data as a basis for Investment Plan determinations in DSUD. Generally, however, AID staff report that data from internal agency accounting systems meet fairly high standards for reliability (no doubt in part motivated by the fact that they will be subjected to a rigorous subsequent audit by COA).

Agencies and the Type-of-Investment Criterion. Expenditure data were submitted by four government corporations and one central government department: (1) the National Housing Authority (NHA); (2) the National Housing Mortgage Finance Corporation (NHMFC) for the Community Mortgage Program (CMP); (3) the Metropolitan Waterworks and Sewage System (MWSS--which operates only within the National Capital Region); (4) the Local Waterworks and Utilities Administration (LWUA); and (5) the Department of Public Works and Highways (DPWH--the one GOP department).

As indicated by the titles on Table 6.1, all of the reported investments fall in definitionally eligible categories: i.e., expenditures for shelter or shelter related infrastructure. NHA expenditures are for sites and services shelter schemes, slum upgrading, median-rise NHA produced finished housing, and housing resettlements schemes. NHMFC data are all for the CMP (which was described in Section 4). MWSS and LWUA investments were made for water supply and sanitation improvements. DPWH investments include water supply as well as flood control, drainage, access roads, and combined urban infrastructure schemes.

¹¹By U.S. law, the local currency equivalent of 100 percent of all funds borrowed under the HG program must be spent on projects that satisfy the first three criteria listed above. It is recognized that it would be prohibitively expensive to actually field-verify the compliance of all projects ahead of time--therefore, some reasonable proxy indicators of eligibility have to be applied in evaluating compliance prior to a borrowing. The DSUD Program Agreement requirement was set at 125 percent to provide a reasonable safety factor in case subsequent audits show that some claimed expenditures were in fact not eligible.

Table 6.1
INVESTMENT PLAN - WORKING TABULATIONS - 1990

Million of Pesos				
Agency or Dept./Eligible Activity:	Disbursements	Attributed to C. Cities	% Below Media	Eligible
National Housing Authority (NHA)				
Sites and Services	37.2480			
Slum Upgrading	9.2620			
Medium Rise Housing	87.9070			
Resettlement	6.6260			
Total	141.0430	100	100	141.043
Community Mortg. Prog.				
Disbursement Vouchers	118.1025	100	100	118.1025
Metropolitan Waterworks/Sewage Sys.				
MIA Water Supply Proj. II	3.7500			
MIA Water Supply Proj. III	3.7600			
MM Sewerage Sanitation Proj	7.1800			
MIA Water Supply Rehab Proj. I	172.4400			
MM Water Distribution Proj	125.3300			
MM Supply Rehab Proj. II	180.4900			
Locally Funded Proj. II	81.5800			
Total	574.5300	56	50	160.8685
Dept. of Pub Works and Highways				
Level I Water Supply	174.1560			
Flood Control and Drainage	108.8180			
Barangay Roads	234.4586			
Urban Development	3.5800			
Total	521.0126	100	50	260.5063
Local Waterworks Utilities Adm				
Total LWUA	66.3306	100	60	33.1653
GRAND TOTAL	1421.018			713.6856 Millions of Pesos

Source: Agency or department special tabulations.

Table 6.2
Investment Plan Expenditures by City and Agency (1990)

	TOTAL	NHA	Thousands of Pesos			MWSS
			CMP	DPWH	LWUA	
NATIONAL CAPITAL REGION						
Manila	105,466	94,401	605	10,460	0	0
Quezon	46,723	12,346	28,313	6,064	0	0
Caloocan	29,850	15,606	12,238	2,006	0	0
Pasay	34,402	0	3,112	1,440	0	0
Total	761,121	122,353	44,268	19,970	0	574,530
LUZON						
Angeles	49,446	0	38,551	10,048	847	0
Olongapo	8,414	0	0	7,990	424	0
Batangas	1,363	0	0	1,337	26	0
Baguio	16,538	0	0	9,014	7,524	0
Cabanatuan	13,967	0	521	12,551	895	0
San Pablo	8,396	989	0	6,352	1,055	0
Lipa	5,172	0	0	2,979	2,193	0
Lucena	11,048	0	0	11,048	0	0
Dagupan	4,365	0	0	4,752	2,262	0
Legaspi	14,113	0	0	10,164	3,949	0
Naga	5,207	842	0	4,146	219	0
Roxas	5,577	0	0	3,066	2,511	0
Puerto Princesa	8,692	0	0	8,652	40	0
Cavite	1,971	0	0	1,971	0	0
Laoag	4,302	0	0	3,258	1,044	0
San Jose	13,352	0	0	12,924	428	0
Iriga	4,384	0	0	4,227	157	0
Tagaytay	1,517	0	0	1,496	21	0
Palayan	3,181	0	0	3,145	36	0
Trece Martires	1,512	0	0	1,512	0	0
Total	182,599	1,831	39,072	120,632	25,721	0
VISAYAS						
Cebu	17,589	3,428	2,107	12,054	0	0
Mandaue	3,945	0	1,404	2,541	0	0
Lapu-Lapu	855	0	0	855	0	0
Danao	3,425	0	3,425	0	0	0
Bacolod	29,537	4,175	0	17,590	7,772	0
Iloilo	15,648	1,273	0	14,068	307	0

Table 6.2 (Continued)
Investment Plan Expenditures by City (1990)

	TOTAL	NHA	Thousands of Pesos			MWSS
			CMP	DPWH	LWUA	
Cadiz	4,238	0	0	4,230	8	0
Tacloban	6,438	0	0	6,137	301	0
Ormoc	15,550	0	0	15,550	0	0
San Carlos	3,122	0	0	3,000	122	0
Bago	3,520	0	0	3,520	0	0
Toledo	3,026	0	0	3,026	0	0
Calbayog	18,327	0	0	17,558	769	0
San Carlos	2,032	0	0	1,910	122	0
Silay	2,890	0	0	2,890	0	0
Dumaguete	3,337	0	0	3,337	0	0
Bals	2,743	0	0	2,743	0	0
La Carlotta	2,747	0	0	2,700	47	0
Tagbilaran	7,561	2,153	2,070	3,338	0	0
Carlaon	653	0	0	653	0	0
Total	124,622	11,029	41,519	103,289	8,671	0
MINDANAO						
Davao	81,718	2,830	12,042	59,668	7,178	0
Zamboanga	40,153	0	0	32,948	7,205	0
Cagayan de Oro	23,891	0	0	10,017	13,874	0
General Santos	30,062	0	11,040	18,948	74	0
Butuan	7,666	0	0	5,764	1,902	0
Iligan	18,645	0	0	18,645	0	0
Cotabato	24,376	0	2,352	21,614	410	0
Pagadian	15,006	0	0	14,914	92	0
Surigao	5,086	0	0	5,011	75	0
Marawi	27,666	3,000	3,746	19,520	1,400	0
Ozamis	4,721	0	0	4,707	14	0
Gingoog	8,528.6	0	0	8,528	.6	0
Dipolog	14,088	0	0	13,272	816	0
Dapitan	13,857	0	0	13,638	219	0
Oroquieta	5,300	0	0	5,300	0	0
Tangub	6,902	0	0	6,793	109	0
Total	313,809	5,830	29,180	226,495	33,371	0
GRAND TOTAL	1,421,018	141,043	118,103	521,012	66,330	574,530

Source: Agency or department special tabulations.

The Below-Median-Income Criterion. Two of the contributors to the Investment Plan restrict their programs directly to individuals and families in low-income groups (in all cases, below-median, and in most cases, well below-median): the NHA and the NHMFC. Their programs are either means tested or focused exclusively in existing communities where virtually all residents have low incomes.

The other programs (by MWSS, DWPB, and LWUA) provide services that benefit higher as well as lower income groups, so some estimate of the share received by below-median income households has to be made. Unfortunately, data on the distribution of household income in Philippine Cities is not available. However, DOF staff have noted that a recent survey shows that approximately 60 percent of the households in Philippine urban areas nationwide live below the poverty line.¹² From this, the DOF proposes it would be appropriate to assume that at least 50 percent of the households in the Cities have incomes below the national median, and therefore to count 50 percent of project outlays in these programs as HG-eligible on this criterion.

The Exclusive-of-Donor-Support Criterion. The accounting system of all agencies, except for one, report sources of funds on an individual project-by-project basis. Thus loan or grant funds received from external donors can be clearly excluded in the tabulations. The one exception is LWUA. LWUA records show only that 40 percent of its total revenues are provided by external donors. Therefore, DOF proposes that 60 percent of LWUAs identified project expenditures be counted as HG-eligible on this criterion.

The City-Location Criterion. All agencies but one have provided project data on a City-by City basis (totals by City are presented in Table 6.2), so it is clear what is HG-eligible on this score for these agencies. The exception is MWSS. Its service area (the National Capital Region) contains four Cities and a considerable area outside of the City boundaries. MWSS records do not permit a direct break out of project beneficiaries by location. DOF proposes that the share of MWSS project expenditures accepted as serving the Cities should be the same as the share of the NCR's total 1990 population located in the Cities (56 percent).

Results. In determining whether the DSUD Investment Plan requirement has been met, the GOP and AID have agreed to convert eligible peso expenditures to dollars on a quarterly basis, using the average daily exchange rate for the quarter. At the time of this assessment, the agencies had not yet provided quarterly breakdowns of the totals shown in Table 6.1 (they expect to provide this breakdown to AID shortly). Without the quarterly data, we cannot give the precise dollar equivalent of the P 713.7 million working total, however, a range can be indicated. Using the average exchange rate during 1990 (P 24=US\$ 1) the total converts to US\$29.74 million, 148 percent of the proposed US\$20 million first tranche. Using the exchange rate at the end of the year (P 26.76=US\$ 1) the total is the equivalent of US\$26.67 million, 133 percent of the first tranche target. In

¹² As noted in Section 2, there are many urban areas outside of the Cities and not all of the populations of the Cities are urban. The data that are the basis for the poverty estimate were derived from the 1988 Family Income and Expenditure Survey (FIES). In this survey, the incomes of individual families are set against a national norm and adjusted for family size in order to determine poverty status. The survey was administered to a sample of approximately 17,000 heads of households and is now being conducted every three years.

either case, the amount exceeds the \$25 million that would be required as per the Implementation Agreement. Therefore, assuming that the information provided is properly certified, the GOP should be able to meet the Investment Plan requirement for the first tranche as planned.

FUTURE IMPROVEMENTS

Plans developed by DOF and AID staff during this assessment promise a more systematic approach for the submission and review of DSUD Investment Plan data in the future. A form has been devised and agreed upon by which each agency will record their data on a quarterly basis and submit the data with signature as evidence of authenticity. DOF staff will regularly assemble the expenditure data from the agencies, critically examine all data presented, negotiate improvements as appropriate, and submit full reports to USAID/Manila.

Also, while we have no basis for questioning the estimating methods proposed by GOP at this time, it should be possible to improve all of these methods in the future: (1) LWUA could develop a system to record donor contributions on a project-by-project basis; (2) MWSS could develop a method for more accurately measuring the peso value of its investments in and outside of the NCR Cities; and, most important, (3) more analysis could be done to support better estimates of the share of project-by-project benefits (for all agencies except NHA and NHMFC) that are likely to accrue to below-median income households in different Cities. Options with respect to the latter include more research on data by location provided by consumer expenditure surveys, and mapping analysis (showing the spatial relationships between service networks and low income neighborhoods) in selected Cities.

Section 7

**CONSTRAINTS AND OPPORTUNITIES
TO STRENGTHEN THE PROGRAM**

In this Section we look across program elements to describe what the assessment team considers to be the highest priority constraints and opportunities facing DSUD at this point, and make recommendations for addressing them. Most of the basic recommendations offered here are endorsements of suggestions made by Philippine officials (central and local) and others interviewed during the assessment. Although we embellish them with our own thoughts in some cases, the basic ideas are already being considered locally.

The Section opens with a brief review of the context and suggests two overriding themes for guiding the next stages of DSUD. It then goes on to examine constraints and opportunities in four areas.

THE CONTEXT

Decentralization is already an urgent requirement for Philippine development. If a new *Local Government Code* is passed with implementation required in six months, the urgency and the challenge will be magnified substantially.

Obviously, the most important task will be to markedly strengthen local governments so they can perform their new responsibilities effectively. The passage of a new law alone will not automatically create effective performance. Philippine local governments are not performing all of the functions they have the power to perform, or raising all of the revenue they are entitled to raise, even under current laws and regulations.

Why is this the case? Partially, it is because of a number of traditional central government practices (noted throughout this report) that reduce their incentives to take

charge, and because they lack resources. Many of these constraints should be addressed by serious implementation of the new *Code*. Clearly, however, it is also due to the fact that the local administrations lack adequate staff, systems and procedures.

Of course, truly sufficient strengthening of local capacity cannot be expected to occur in six months. However, significant progress on this front will be required very soon. Otherwise, failures in the overall system of government could deter progress toward the nation's fundamental social and economic objectives. Movement toward a market-oriented economy implies that government should shift out of some of its past activities, but the functions that remain are vital to a well functioning private market and to social progress (ranging from the efficient administration of the nation's system of laws to the delivery of basic infrastructure and public services).

Recent literature examining the decentralization experiences of many countries around the world (see, for example, Rondinelli, 1990, and Peterson, et al, 1990) offer two lessons that are relevant here. First, decentralization has proceeded in a number of countries by continuing political conflict between central bureaucracies (attempting to hold on to power) and popularly elected Mayors, in which the Mayors gradually gain the upper hand (e.g., this appears to be happening in much of Latin America). The problem with this mode is that it is time consuming. The Philippines does not have the time for it. A first theme of this section, then is that:

The next stages of decentralization must take place as a truly cooperative and well coordinated effort on the part of central and local governments--one characterized by frequent and open exchanges of views in a settings designed to bring harmony and motivate progress.

The second lesson is that central governments appear to be as unable to design local capacity building effectively as they are unable to deliver local services effectively. Experiences throughout the world over the past decade indicate that even well-intentioned efforts by central governments to plan decentralization in detail are doomed to failure. The central Ministries of Home Affairs or Local Government simply cannot know enough about the varying circumstances and priorities of different localities to design workable manuals. Our second theme, then, is:

The job of strengthening effective local performance capacity must rest with the localities themselves, and the job of central staff must be to facilitate their efforts in that role.

1. EXPEDITING THE DEVELOPMENT OF STREAMLINED GUIDELINES FOR IMPLEMENTATION

Our first recommendation for DSUD is that the very highest priority be given to supporting DILG and the Cities in the development of streamlined guidelines for the implementation of the new *Code*. Once it is passed, nothing could threaten its success more than confusion about the way it is to be implemented. Even local governments with substantial capacity will be held back if they do not have written guidelines that clarify their legal powers and responsibilities in an exact manner. Obviously, the work on basic implementing guidelines and regulations must be done with considerable speed.

The word "streamlined" is extremely important here, consistent with the themes noted above. The term "enabling" could also have been used. The point is that central agencies must resist the temptation to get into too much detail in these basic implementing documents. The guidelines should clarify in simple and direct language what local governments have the responsibility to do and they should avoid trying to set forth elaborate statements on how it is to be done. More detailed manuals on the latter are needed, but they can best be developed by the localities themselves, with appropriate technical assistance, to fit their own circumstances (see recommendations under 3 below).

The DILG has drafted statements of work for developing a conceptual framework for the decentralization process at the central level along these lines and, in particular, for drafting circulars and guidelines accordingly. This work should be given the highest priority. So far, however, an important ingredient is missing. Again, consistent with the themes noted earlier, a process of collaboration with local officials needs to be built into the design of the guidelines from the start. Feedback from the local leaders who will have to live with them will be essential if the guidelines are going to be workable in a short period of time. Processes for securing such collaboration are discussed under the next two objectives.

2. BUILDING A FORCEFUL COALITION OF CENTRAL AGENCIES AND AN EFFECTIVE COORDINATION PROCESS.

We believe there is now a need for more frequent meetings at the central level to coordinate the decentralization process. It is particularly important to involve the DSUD group of agencies together, since they all represent various aspects of the physical development process and this aspect needs this sort of forum. (Several agency representatives interviewed during the assessment suggested this was needed).

Committee meetings should be scheduled on a regular basis. In each: 1) agency representatives would review the progress they have made toward stated objectives and discuss the problems and constraints they face; (2) other attendees would comment and offer suggestions; and (3) adjustments would be made to interim assignments and technical assistance priorities under each objective.¹³

This sort of a process creates pressures for more timely performance. More important, it can build positive and strong interagency ties and comraderie which will be needed during the pressured times that lie ahead. One of the most important opportunities to improve its effectiveness would be to invite representatives from the Leagues of Provinces, Cities, and Municipalities to serve as regular participants.

It would be unreasonable, however, to develop this sort of process for DSUD alone. At the minimum, the process should combine the actions specified under both DSUD and LDAP and become a part of (rather than operate separately from) the overall process that will be established to implement the code (whether managed under a continuation of

¹³ Processes for effective collaboration of central agencies in the decentralization process are being developed for other countries. One of the most prominent is the work of *Tim Koordinasi* in Indonesia (see Tjahjati, 1990 and Tim Koordinasi 1987 and 1990).

CDIT or any other entity created for this purpose). It will be important that the participants in this process devote the time needed to follow-through on the details of the agenda; i.e., that it become a true "working coalition". If CDIT itself involves officials at too high a level to play this role, one or more subcommittees may be needed.

3. A "DEMAND DRIVEN" SYSTEM FOR STRENGTHENING LOCAL CAPACITY

The most vital need in decentralization at this point is strengthening capacities at the local level. There is a need to reach agreement soon about the process by which this strengthening will take place.

Consistent with the themes discussed above, an approach almost certain not to work is for central agencies to try to plan this process in detail and then enforce local governments participation. There are two major risks. First, central agencies are not likely to be able to sensitively address the diversity of real local priorities and will thus waste resources on efforts that do not match true demands. This is the same as one of the most fundamental realities that drives the decentralization of service delivery--central agencies simply cannot know enough to set priorities and standards for all this complexity in a rational way, and they do not have the right incentives to do so even if it was technically feasible. Second, because they do not feel that a centrally design capacity strengthening process is "their own", local leaders are certain to criticize it and not take its implementation seriously no matter how well it is designed.

We believe the approach most likely to succeed is one in which central officials facilitate a process by which the Cities themselves design and carry out the strengthening of their own capacities. The needs for stronger capacity among the Philippine Cities are uneven. Some City governments are generally stronger, more entrepreneurial, and more effective than others. There are many examples of impressive achievements in recent years by the Cities themselves (e.g., new computer systems, new methods of raising revenue or privatizing services). The Cities can do much to help each other.

To operationalize this approach, technical assistance and training resources (from DSUD and other sources) should be made available to the League of City Mayors (under a clear contractual arrangement that sets fair expectations on both sides). The League would probably have to set up a new technical directorate to manage and coordinate this activity. The League would hold more frequent conferences and seminars with its members. Mayors and other officials would be encouraged to talk together about their most pressing problems, opportunities, and objectives.

The context would be such that advisors in these meetings would help the Mayors to match assistance resources and modes of delivery to the priorities that are exposed in these discussions. The most cost-effective means in many cases may be for the officials of some Cities to copy a success story from one of their other sister Cities. After a Mayor and his or her staff have assessed their own most urgent needs, they are likely to know best how to select services. In some cases, the best approach may be simply to support staff from a City that has implemented a successful innovation to give seminars and training courses (and make reports and manuals available) to the staffs of other Cities. In other cases, it will be most appropriate to choose a course from a local university. In others, the best response may be for three or four Cities to pool resources and hire a

consulting firm to design and install a new system. In yet others, it may be most appropriate to choose a training course or operational manual developed by a central agency, bringing in outside technical assistance support as needed. There are strong advantages in maintaining an environment of competition among the potential providers of technical assistance and training.

Central agencies should play a strong, but mainly supportive, role in all of this. First, in all their actions, they need to evidence a willingness to serve as cooperative partners in this "bottom up" type of approach. Second, they should systematically monitor its progress and providing feedback to suggest opportunities for program enhancement where it is most needed. (In many cases, simply the regular publication of comparative statistics on changes in local conditions and performance for all cities individually, will be the strongest motivator). Third, central agencies should support broader research on changing urban conditions and some developmental research (e.g., systems to address common problems). These are tasks where economies of scale make a difference--individual cities cannot normally afford them. Finally, central agencies should develop some new training courses and operate systems for priority needs. However, the decisions about what specific technical and assistance and training should be offered by the central government should be worked out in close collaboration with the League of City Mayors and build only in areas where the central government has a competitive advantage as a provider. Their products in this regard can and should be forced to compete with those offered by other private and public capacity building providers.

One example for consideration is the decentralization program of the Department of the Environment and Natural Resources (DENR) where central government provincial officers play an important role, but they act more as facilitators of the work of their local government counterparts, rather than supervisors.

4. URBAN PHYSICAL DEVELOPMENT AS A FOCUSING THEME FOR DSUD RESOURCES

Considering the objectives of the broader GOP program, it seems reasonable to view the current DSUD Policy Matrix as a starting point rather than a definitive statement of all things DSUD could contribute to decentralization in the Philippines. As the program evolves it should be possible to integrate activity across program elements to enhance accomplishments.

Elements for Integration. A central theme of DSUD that distinguishes it from LDAP and many other aspects of decentralization, is that it focuses on the *physical development of the City*; i.e., its functional specialties relate to urban services, infrastructure, land, shelter, and physical planning. This could be an important theme for the deployment of DSUD technical assistance and training resources. Particularly important in this mix are the two key DSUD elements that relate to the strengthening of the process for budgeting and programming infrastructure improvements (i.e., the Capital Investment Folio approach noted under objective 2c) and the updating of town plans (under objective 3a). Urban master plans have often failed because they have not offered adequate guidance to action programming (see discussion in Section 5). Capital budgeting has often run into problems when it has not been guided by some sort of

spatial plan for a city that facilitates the geographic coordination of investment; i.e., the capital program can become simply a "collection of projects", without serious funding plans (see discussion in Section 4).

Furthermore, a good spatial framework plan can much simplify the processes of project identification and appraisal. If sufficient economic and cost analysis is provided to back it up, the plan provides substantial background data and reasoning to support the selection of projects without requiring elaborate and time-consuming appraisals for each project individually; i.e., the program as a whole is appraised in economic terms and individual component projects can be justified with little additional analysis.

Similarly, the work on building inventories of public land (objective 3a), the design of innovative but economically viable means of credit financing for infrastructure (objective 1c), the development of approaches to cost recovery and privatization in infrastructure provision (objectives 2a and 2b), and the programming of NHA joint-venture and CMP resources in a city (objectives 3b and 3c) are all closely related to the town and capital investment planning processes. Their contributions should be enhanced if the such relationships between elements are thought through carefully ahead of time.

Finally, an goal that runs through many elements of DSUD (but is not a separately identified objective) is environmental protection (sustainable development) as the process of urban physical development proceeds. Actually, this is appropriate. Environmental concerns cannot be addressed effectively by a "separate activity". Rather, environmental implications must be assessed and dealt with forcefully within each element of physical planning and implementation.

A Possible Scenario for Technical Assistance and Training to Strengthen City Capacities. How could this idea be operationalized? A series of steps is suggested below to illustrate the possibilities.

1. As a part of the process of "demand driven" capacity strengthening (recommendation 3), the League of City Mayors would meet with AID DSUD representatives and representatives of the central coordinating committee (recommendation 2), to work out a basic approach for integrating the planning and implementation of urban physical development. On the basis of some analysis of comparative needs and capabilities, several Cities would be selected as places to try it out. (Actually, several meetings would be required with some consultant assistance in-between).

2. Technical assistance teams would then arrive to work with officials of the selected cities to implement the model approach. (The TA teams might include staff from other Cities and central agencies as well as consultants). The first meetings would develop a work program and schedule and clarify assignments.

3. The first step in the process would be to conduct analyses of the City's conditions and prepare a simple spatial framework plan for the City's future development. The approach would vary depending on what information the City already has on hand; e.g., data on demographic, economic, and land use trends for sub-areas. Even where data is sparse, new techniques (e.g. quick interpretation of satellite images, numerous

analytic software packages) permit much more rapid and inexpensive work of this kind. The complete inventorying of lands owned by all levels of government within the City would be a key element at this stage.

4. In preparing the plan, results of the analysis would be presented to a broad committee of local leadership (the local Development Councils with representation from NGOs and other private leaders as well as local government) are ideal for this purpose. It is important that local public works and budget staff participate actively--they will have to live with the decisions that are made and their participation will give them personal stake in the outcomes. (Physical planning is much too important to be left solely to physical planners). For a more complete discussion of approaches to this sort of framework (or "structure") planning see Kingsley, 1991, and Peterson, et al, 1990).

5. Once a broad framework plan is developed, the Local Development Council and technical assistance team should move immediately to considering its implications for the capital budget (no need to wait for any official "adoption" of the plan). The Capital Investment Folio approach (or some appropriate modification) offers solid guidelines for this phase. The framework plan offers the most rational basis possible for assessing priorities and internal consistencies in the capital budget, across sectors and across the spatial terrain of the City. At the same time they should consider actions other than capital projects that may be necessary for achieving the type of development called for in the framework plan; i.e., streamlining development records, deployment of government owned land, establishing environmental protection approaches.

6. A clear imperative is that a financing plan (evaluating all potential sources of funding) be prepared at the same time as capital projects are being prioritized (the logic of this was explained in Section 4). This--the comparison of assembled costs of projects you want to implement with potentially available funding--is the process that should force local leadership to recognize the need to enhance tax generation and use new sources of funds (e.g., bonds and other creative approaches to borrowing). It should be remembered at this time as well that the selling of idle public lands to private users can be an extremely effective means for raising funds to support capital development. Cost recovery and privatization also will have to be considered and planned for in these deliberations.

7. These planning/programming/budgeting efforts in the selected cities would be carefully monitored and evaluated. The results would be presented back to the League of City Mayors on a regular basis as the process is going on and feedback gained in this forum should be used for mid-course corrections. After the processes are well advanced in the first round of Cities, guidelines and manuals might be developed and sent to other Cities. A second round would then be designed, hopefully requiring much less in the way of technical assistance resources per City than the first.

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Annex B

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