

# The Philippine Water Revolving Fund Support Program

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## REVISED YEAR 2 WORKPLAN

February – September 2008



This project is implemented by Development Alternatives, Inc. in association with:

- The Community Group International LLC
  - Resource Mobilization Advisors
    - CEST, Inc.



## **PREFACE**

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The United States Agency for International Development (USAID) Philippine Mission has contracted Development Alternatives Inc. (DAI) to implement the Philippine Water Revolving Fund Support Program (PWRF) under contract number EPP-I-00-04-00023. The effective date of the contract is October 1, 2006. DAI is implementing the project in collaboration with TCG International, LLC, Resource Mobilization Advisors and Consultants for Engineering Science and Technology, Inc.

USAID extended the base year by six (6) months, i.e., to March 31, 2008 and exercised the option period to September 30, 2011. The team submitted the Year 2 Work Plan in August 2007, revised it in December 2007 and again now to ensure responsiveness to the emerging priorities of the client. USAID advised the team to be agile-- quick to capitalize on opportunities, as well as quick to adjust to new constraints in the operating environment. This revised work plan presents the long-term objectives and strategic direction of the Life-of-Project Plan but covers an 8-month period, February to September 2008 only in terms of the specific activities and expected outputs. This work plan was prepared in consultation with our Cognizant Technical Officer and with the Chief of the Office of Energy and Environment of USAID.

Alma D. Porciuncula  
Development Alternatives Inc.  
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## TABLE OF CONTENTS

<b>INTRODUCTION .....</b>	<b>1</b>
<i>TAKING STOCK OF THE PWRf INITIATIVE.....</i>	<i>1</i>
<i>WAY FORWARD.....</i>	<i>2</i>
<b>COMPONENT 1: PWRf INSTITUTIONAL DEVELOPMENT.....</b>	<b>4</b>
OBJECTIVE.....	4
COMPONENT 1 DELIVERABLES.....	4
PLANNED ACTIVITIES .....	4
1.1 <i>Action Memorandum for the DCA-LGUGC Guarantee Agreement.....</i>	<i>4</i>
1.2 <i>Technical Assistance on Securitization of LWUA Receivables.....</i>	<i>4</i>
1.3 <i>Assist Water District/s with a Bond Transaction.....</i>	<i>7</i>
1.4 <i>Concept and Design of a Long-term Financing Mechanism.....</i>	<i>8</i>
1.5 <i>Continuing Training to PFIs and other PWRf Stakeholders on Water Project Appraisal.....</i>	<i>8</i>
1.6 <i>Water Project Appraisal Guidebook for Lenders.....</i>	<i>9</i>
1.7 <i>Institutional Support to DBP for the PWRf Lending Window.....</i>	<i>9</i>
<b>COMPONENT 2: WATER/SANITATION PROJECT DEVELOPMENT .....</b>	<b>11</b>
OBJECTIVE.....	11
COMPONENT 2 DELIVERABLES.....	11
PLANNED ACTIVITIES .....	11
2.1 <i>Assist Utilities to Update Feasibility Studies and Prepare Projects for PWRf Funding on Demand Basis.....</i>	<i>11</i>
2.2 <i>Feasibility Assessment and Design of the Project Development Facility.....</i>	<i>12</i>
2.3 <i>Implementation Guidelines of the LWUA-administered Project Development and Efficiency Improvement Program.....</i>	<i>12</i>
2.4 <i>Feasibility Study and Business Model for Water Districts on Septage Management .....</i>	<i>12</i>
2.5 <i>LGU Training on WSS Project Development.....</i>	<i>13</i>

<b>COMPONENT 3: WATER AND FINANCE SECTOR STRENGTHENING .....</b>	<b>14</b>
OBJECTIVES .....	14
COMPONENT 3 DELIVERABLES.....	14
PLANNED ACTIVITIES.....	14
<i>3.1. Prepare a policy paper on the rationalization of public resource allocation for water supply and sanitation projects.....</i>	<i>14</i>
<i>3.2 Support DOF to put in place financial incentives for water sector lending.....</i>	<i>15</i>
<i>3.3 Technical assistance to DOF for the coordination of water sector reform agenda (through the water sub-committee of the Philippine Development Forum).....</i>	<i>15</i>
<i>3.4 Conference on regulatory reform for water supply and sanitation.....</i>	<i>16</i>
<i>3.5 Assist Water Utilities in Preparing Business Plans.....</i>	<i>16</i>
<b>COMPONENT 4: GENERAL PWRf PROGRAM SUPPORT .....</b>	<b>17</b>
OBJECTIVE.....	17
COMPONENT 4 DELIVERABLES.....	17
PLANNED ACTIVITIES.....	17
<i>4.1 Provide technical secretariat support to the PWRf Steering Committee and Technical Working Group.....</i>	<i>17</i>
<i>4.2 Provide Support to USAID's Reporting, Advocacy and Collaboration with JBIC on the PWRf.....</i>	<i>17</i>
<i>4.3 Knowledge/Information Dissemination and Management.....</i>	<i>17</i>
<b>OPPORTUNITIES FOR COLLABORATION WITH USAID AND OTHER DONOR PROJECTS ...</b>	<b>18</b>
FIGURE 1: PWRf YEAR 2 WORK PLAN.....	20
<b>BUDGET .....</b>	<b>25</b>
ANNEX 1 .....	27

## Introduction

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### *Taking Stock of the PWRF Initiative*

USAID's primary objective in supporting the development of the water revolving fund in the Philippines is to improve access to safe drinking water and sanitation by stimulating investments through the establishment of a sustainable financing program. The PWRF development effort rides on the US-Japan collaboration under the Clean Water for People Initiative. USAID's technical assistance on the development of the revolving fund and its credit enhancement of private financing institution loans through the Development Credit Authority would be complemented by JBIC's loan funds to capitalize the fund. The loan will be made to the Development Bank of the Philippines, which will then re-lend it to water utilities with co-financing from commercial banks or private developers. The co-financing of direct loans is then planned to transition to capital market-based instruments such as securitization of the loan portfolio and/or pooled bond financing for new projects.

The PWRF Support Program's work plan was based on this implementation framework. The key result areas of the PWRF-SP focus on:

- Operationalization of the PWRF
- Project development for PWRF financing
- Policy reforms to support viability of PWRF
- Capacity building for better utility management
- Capacity building of lenders on water supply and sanitation financing

However, the key underlying conditions have changed, i.e., the delay of the JBIC loan and new developments in the market warrant a second look at the implementation framework. The JBIC loan was expected to be committed in March 2007. While in process, it was also assumed that DBP will use its second generation funds from a previous JBIC loan for the PWRF co-financing arrangement. Both did not materialize. Nonetheless, the Program's efforts to familiarize private financing institutions with the sector, bolstered by the high liquidity in the market and low interest rate regime, have borne fruit. PFIs, with the assistance of LGUGC originated loans on their own and financed water supply projects 100% or co-financed with LWUA, with LWUA taking on only a 10% share. Moreover, LWUA has agreed to try securitization of its receivables. This could potentially deepen LWUA's foray in working with the private finance market. It could also attract participation of new players such as insurance companies.

Furthermore, the insights gained from the US study tour on water revolving funds brought about a new perspective on the rationalization of financing resources. It also highlighted the need for effective regulations that will compel the water utilities to achieve 100% service coverage and meet environmental and performance standards. It is opportune that there are on-going parallel regulatory and institutional reform efforts that the Department of Finance (DOF), PWRF's lead GOP partner, is also involved in. DOF has taken the initiative of organizing a coordinating group that will prioritize the overall sector reform agenda, as well as ensure complementation of efforts of all players involved. DOF has requested USAID technical assistance in this regard; and this will be delivered through PWRF-SP.

Thus far the PWRF development process has raised awareness of PFIs on water projects as viable investment alternatives. In the same vein, it also raised awareness of LWUA on the merits of partnerships with private financing institutions and encouraged it to venture on capital market mechanisms. It has also gotten traction with its advocacy to the Department of Finance to exercise its leadership role in the water sector reform agenda. DOF has opened wider possibilities for

providing national government support for the sector’s financing, which then open up new avenues for financing. For a start, it facilitated a PhP 250 million subsidy to LWUA in December 2007 to specifically finance project preparation and efficiency improvement projects that will help water districts improve their creditworthiness. DOF is also more pro-active in pushing forward other reforms realizing that financing alone will not generate investments or improve performance, rather should be complemented with other drivers such as regulations, empowered constituency, or even peer group benchmarking.

**Way Forward**

USAID reiterated its core objective for the program and its commitment to the JBIC collaboration; but in the same breath clarified its intent to support financing reforms with or without the JBIC loan, as manifested by the renewal of the DCA guarantee agreement with LGUGC. It appreciates the evolving operating conditions and as such advised the team to be focused on the long-term objective but ready for tactical shifts to build on emerging opportunities, respond to GOP priorities and adapt to constraints beyond the program’s ability to address.

USAID and team agreed the program’s strategic framework, as shown below:



The major revisions in the Year 2 work plan as agreed with USAID are:

- Re-focus Component 1 on the development and piloting of capital market-based financing schemes, such as the securitization of LWUA receivables; nonetheless keep a place holder for the institutional support to DBP for the co-financing arrangement once the JBIC loan is committed;
- Re-orient the approach of Component 2 on project development; instead of actively identifying projects and offering technical assistance for improving pre-investment studies, provide the technical assistance on demand basis; assistance could be provided to projects in the pipeline of DBP or LGUGC; invest greater effort in long-term enablers for project development, specifically capacity building of LGUs on project development and institutionalizing a project development facility;
- Under Component 3, add a policy analysis on the rationalization approach for resource allocation; in EO 279, the government subsidy will be allocated on the basis of creditworthiness; the policy analysis will review if this premise responds to the long-term goal for the sector. In particular, allocation of government subsidy, as in the case of US Revolving Funds, may be on the basis of development objectives, such as compliance with standards of the Clean Water Act.

The following are the expected outputs under the Year 2 work plan:

<p>Component 1 PWRf Institutional Development</p>	<ul style="list-style-type: none"> <li>▪ Action Memo to DCA requesting approval of its Credit Review Board on the new guarantee agreement with LGUGC</li> <li>▪ TA to LWUA for the securitization of its receivables</li> <li>▪ On demand basis, TA to a water district for a bond issuance</li> <li>▪ Concept and Design of a long-term financing mechanism (informed by the result of the policy analysis on resource allocation)</li> <li>▪ Training Workshops for PFIs and PWRf Partners on Water Project Appraisal</li> <li>▪ Water Project Appraisal Guidebook for Lenders</li> <li>▪ Subject to JBIC loan commitment, institutional support to DBP to establish PWRf lending window</li> </ul>
<p>Component 2 Project Development and Capacity Building of Utilities</p>	<ul style="list-style-type: none"> <li>▪ On demand basis, TA to water utilities to update or upgrade pre-investment studies</li> <li>▪ Feasibility Assessment and Design of a Project Development Facility</li> <li>▪ Implementation guidelines for the LWUA-administered Project Development and Efficiency Improvement Fund</li> <li>▪ Feasibility analysis of septage management and preparation of a business model for water districts</li> <li>▪ LGU training program on WSS project development</li> </ul>
<p>Component 3 Water and Finance Sector Strengthening</p>	<ul style="list-style-type: none"> <li>▪ Policy analysis on the rationalization of public resources for water supply and sanitation investments</li> <li>▪ Financial incentives for WSS lending</li> <li>▪ Technical support to DOF for its leadership in the sub-committee for water under the Philippine Development Forum</li> <li>▪ Conference on regulatory reform for water supply and sanitation</li> <li>▪ Training and institutionalization of business planning among water utilities</li> </ul>
<p>Component 4 General Program Support</p>	<ul style="list-style-type: none"> <li>▪ Overall program support to USAID and its collaboration with JBIC</li> <li>▪ Technical secretariat support to the PWRf Steering Committee</li> <li>▪ Knowledge management tool: PWRf website</li> </ul>

## **Component 1: PWRF Institutional Development**

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### **OBJECTIVE**

Develop and pilot capital market-based financing mechanism for water supply and sanitation projects; and subject to commitment of JBIC loan to DBP, provide institutional support to establish and operationalize the PWRF lending window in DBP.

### **COMPONENT 1 DELIVERABLES**

- Action Memo to DCA requesting approval of its Credit Review Board on the new guarantee agreement with LGUGC
- TA to LWUA for the pilot transaction securitization of its receivables
- On demand-basis, TA to a water district for a bond issuance
- Concept and Design of a long-term financing mechanism (informed by the result of the policy analysis on resource allocation)
- Training Workshops for PFIs and PWRF Partners on Water Project Appraisal
- Water Project Appraisal Guidebook for Lenders
- Subject to JBIC loan commitment, institutional support to DBP to establish PWRF lending window

### **PLANNED ACTIVITIES**

#### **1.1 Action Memorandum for the DCA-LGUGC Guarantee Agreement**

The USAID Mission has to prepare an action memorandum in connection with the request for DCA approval of the new guarantee agreement with LGUGC on water supply and sanitation projects. The action memorandum contains the background information, economic and financial analysis and risk assessment, and term sheet for the guarantee agreement. Our team will provide inputs on the situationer, the underlying analysis, and other information required by DCA.

#### **1.2 Technical Assistance on Securitization of LWUA Receivables**

The securitization of receivables is a breakthrough for LWUA, which has traditionally used ODA re-lending scheme; and for that matter the sector's fund sourcing paradigm, which has always been through direct credit. This exercise is significant in the following ways: it will be a great learning experience for LWUA and hopefully will serve as the impetus to sustain its foray in the capital market; it will introduce and test the appetite of the domestic capital market to water investment securities; and it may set the stage for other capital market-based mechanisms such as bond financing. The asset-backed securitization modality, being an outright sale of receivables also circumvents the domestic borrowing capacity limitation of LWUA. As such LWUA achieves liquidity, without increasing its debt stock. There are however trade-offs and pitfalls to the securitization, hence the need to be circumspect and thorough with the analysis.

**Box 1. LWUA Asset Securitization: Introducing Water District Bonds**

LWUA is studying the feasibility of undertaking an asset securitization in order to take advantage of attractive interest rates in the market and improve its balance sheet. As shown in the table below, the cost of funds has markedly declined in recent years. In fact, yields on 10-year Treasury Bonds have been effectively halved since 2005 and now stand at around 6.1%. Lower bond yield makes it attractive for corporations both private and public to raise funds from the capital market (higher bond yields makes it attractive for financial institutions to lend to the National Government).

**Yield on Treasury Bonds (%)**

	2003	2004	2005	2006	Jan 2008
2-year	8.50	10.38	8.88	7.47	5.39
4-year	10.38	11.33	11.25	6.50	5.59
5-year	8.15	11.64	10.95	8.72	5.70
7-year	11.88	11.75	11.25	8.65	5.86
10-year	11.81	12.31	11.69	8.06	6.10
20-year	12.23	13.00	12.13	9.69	8.38
25-year				10.31	8.49

Source: Bureau of Treasury, [asianbondsonline.com](http://asianbondsonline.com)

Asset securitization is simply one of the ways to raise funds. One way to raise cash is to issue bonds or to borrow from banks. In LWUA's case, its domestic borrowing ceiling of P1.0 billion has already been reached, thus limiting its cash raising ability.

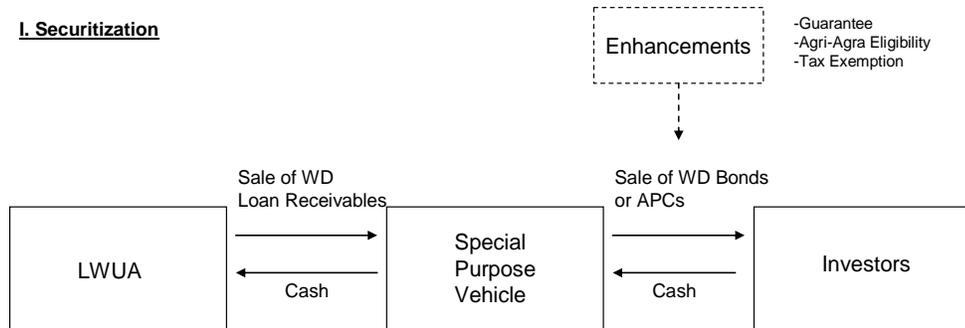
The chart below shows the main difference between asset securitization and a bond issuance. In a bond, the corporation sells debt to the market and gets cash directly. The debt papers then become part of the liability of the issuing corporation. In an asset securitization, the loans from the originator (in this case LWUA) are pooled and sold to a special purpose vehicle (SPV). The SPV could either be a Special Purpose Corporation (SPC) or a Special Purpose Trust (SPT). The SPV then issues either bonds (in the case of an SPC) or asset participation certificates (in the case of an SPT) to investors to get cash to be able to pay the originator. In this case, the loans then become part of the assets of SPV and the bonds become part of its liabilities.

If the capital market reception is positive<sup>1</sup>, an asset securitization will have beneficial effects on LWUA's financial position. First, it can retire its high cost domestic debt which can result to a lower interest expense or it can prepay some of its foreign currency denominated obligations which can lower foreign exchange losses. Securitization can then be a financial tool to better manage LWUA's finances. Second, securitization will introduce Water Districts to the capital market; investors of securities in effect buy loan receivables from WDs. This could have a positive impact on LWUA and the WD's corporate governance, as the market will impose hard credit discipline and greater transparency. Third, a successful securitization will demonstrate to larger WDs that the capital market can be a good alternative source of funding. They may find bond financing an attractive alternative, thus reducing reliance on ODA funded facilities.

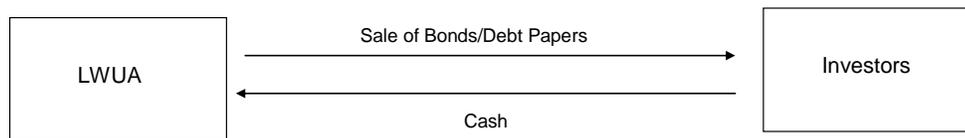
<sup>1</sup> Capital market reception to a water district bond could be significantly influenced by what the National Government could give in terms of incentives to bond or APC holders.

Securitization vs Bond Issuance

**I. Securitization**



**II. Bond Issuance**



Although a securitization will have potential benefits, its success will depend to a large extent on National Government support for its implementation. First, the bonds or the APCs will be compared with other available investment instruments in the market. As such, there is a need for the Government to give comparable incentives to water district bonds.<sup>3</sup> Second, the market needs to be educated on and be comfortable with the sector. In the initial phase of securitization transactions, there might be a need for sufficient incentives to overcome investors' 'initial fear' or unfamiliarity with the sector. Third, in order for securitization to be a sustainable and recurrent activity, the Government must immediately resolve critical regulatory issues that have a bearing on Water District financial performance. An example of this is the impending issue on corporate income tax applied to WDs. Though exempting WDs from income taxes might be the better course from a public resource allocation point of view<sup>4</sup>, it is the predictability of taxation (which will impact on cash flows) and not tax exemption itself which will ultimately concern the bond or APC holders.

<sup>3</sup> An example is the withholding tax exempt status given to housing bonds or asset participation certificates issued with guaranty given by Home Guaranty Corporation.

<sup>4</sup> It is worth noting that Water Districts have received very little support aside from the grants that are channeled through LWUA from the National Government. Though the water sector is as important as housing, the water sector does not receive the same attention from the National Government as the latter.

We have prepared an MOU with LWUA for technical assistance to guide them through the process. Prior to the signing of the MOU, LWUA will seek explicit legal opinion from the Office of the Government Corporate Counsel on its authority to do securitization. LWUA will also review its existing loan agreements with donors to ensure that they do not preclude securitization.

Our technical assistance to LWUA shall cover the following tasks:

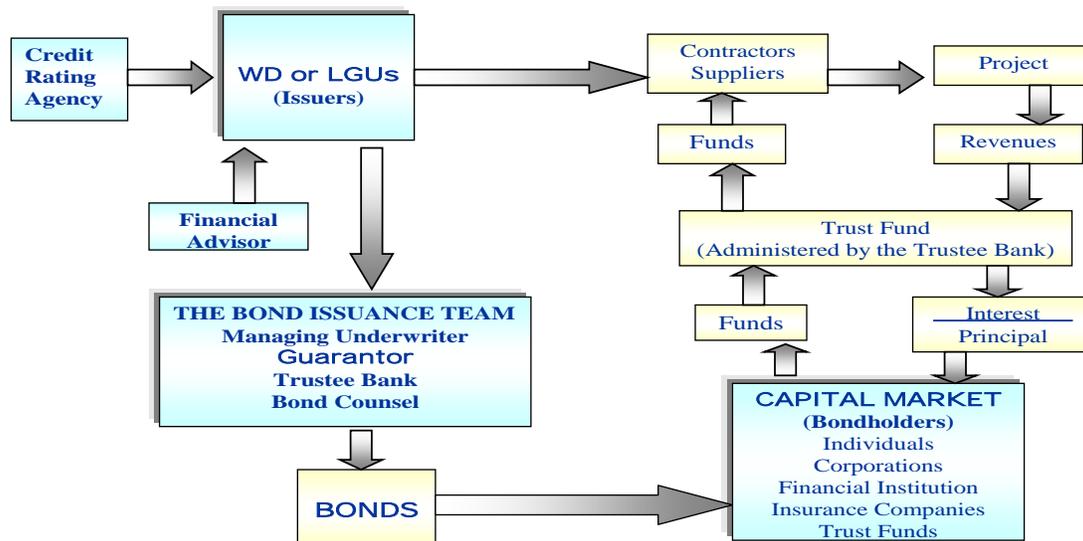
- Assessment of the viability of selling LWUA's pool of water district receivables to the domestic financial market under an asset securitization scheme;
- Implementation plan: i) step by step activities, ii) regulatory requirements, iii) possible enhancements needed for a successful securitization program for water districts; and
- Guidance and assistance to LWUA orchestrate and manage the activities related to the implementation plan

### 1.3 Assist Water District/s with a Bond Transaction

We will review investment programs of target water utilities and explore interest for testing the market for a water bond issue. We will discuss the pros and cons of bond financing with the water utility and walk them through the process and highlight the obligations on their part. Should there be an interested utility, we will assist the water utility with the bond transaction.

Figure 1 below illustrates the process flow of a typical bond issue. We will provide the financial advisory assistance to the issuer and also assist with the identification of the bond issuance team.

**Figure 1: Bond Transaction Process Flow**



Source: LGUGC

#### 1.4 Concept and Design of a Long-term Financing Mechanism

Our team will prepare a concept paper and design of a long-term financing mechanism based on the recommendations of the policy analysis on rationalization of public resources for water supply and sanitation under Component 3. We will also build on the concept paper that we've prepared for pooled bond financing, as well as draw from the experience of LWUA's securitization process.

Part of the financing scheme will be recommendations for a sustainable financing mechanism for sanitation. To date, utilities have focused investments on water supply and have left households to make investments in sanitation infrastructure – mostly septic tanks – to the detriment of the environment. Our team will work with ECOGOV2, PSA and SCOTIA projects to develop business and financing mechanisms for sanitation services. We will explore pooled financing options; inter-LGU collaboration and private sector participation modalities, and assess different approaches to cost recovery for improved wastewater treatment services.

Working closely with DOF, the paper will be crafted to serve as one of the action plans of the water sector roadmap.

#### 1.5 Continuing Training to PFIs and other PWRf Stakeholders on Water Project Appraisal

As part of our earlier effort to build capacity of PFIs for water sector lending, we will continue to conduct the training on familiarization with the water sector and how to appraise water projects. The seminars will provide an institutional overview of the water service industry, as well as provide private financial institutions with the tools to effectively evaluate water projects both on the technical and financial feasibility aspects. The indicative list of topics to be covered is shown in the table below. We will use water sector experts and practitioners to share knowledge, practical experiences and insights to lenders on the relevant issues that are faced by PFIs in undertaking water project financing.

<b>Training Modules on Water Project Evaluation for PFIs</b>	
Module 1	Water Institutions and Regulations in the Philippines
Module 2	Investment Opportunities in the Water Sector
Module 3	Water Tariff Setting in the Philippines :Overview of the Process and Issues
Module 4	Demand and Revenue Projections in the Water Sector
Module 5	Experiences and Issues in Bulk Water Supply Contracts
Module 6	Experiences of LGU-run Water Service Utilities
Module 7	How to Construct a Financial Model of a Water Service Utility
Module 8	Hydrology Risk Assessment
Module 9	System Planning and Cost Estimation of Water Projects
Module 10	Risk Identification and Mitigation in Water Project Financing
Module 11	Operational Efficiency in Water Service Operations

## 1.6 Water Project Appraisal Guidebook for Lenders

To complement the training on water project appraisal, we will prepare a *Water Project Appraisal Guide Book for Creditors and Investors*. Intended to be a collaborative effort with selected PWRF partners, the book aims to provide creditors an easy guide on how to evaluate the technical and financial aspects of water project proposals. The Water Project Appraisal Guidebook will also contain relevant information on the water sector's institutional, policy and regulatory framework in the Philippines.

## 1.7 Institutional Support to DBP for the PWRF Lending Window

Subject to the commitment of the JBIC loan, we will continue where we left off on the institutional support to DBP to set up and support the operations of the PWRF lending window, which will adopt the co-financing arrangement.

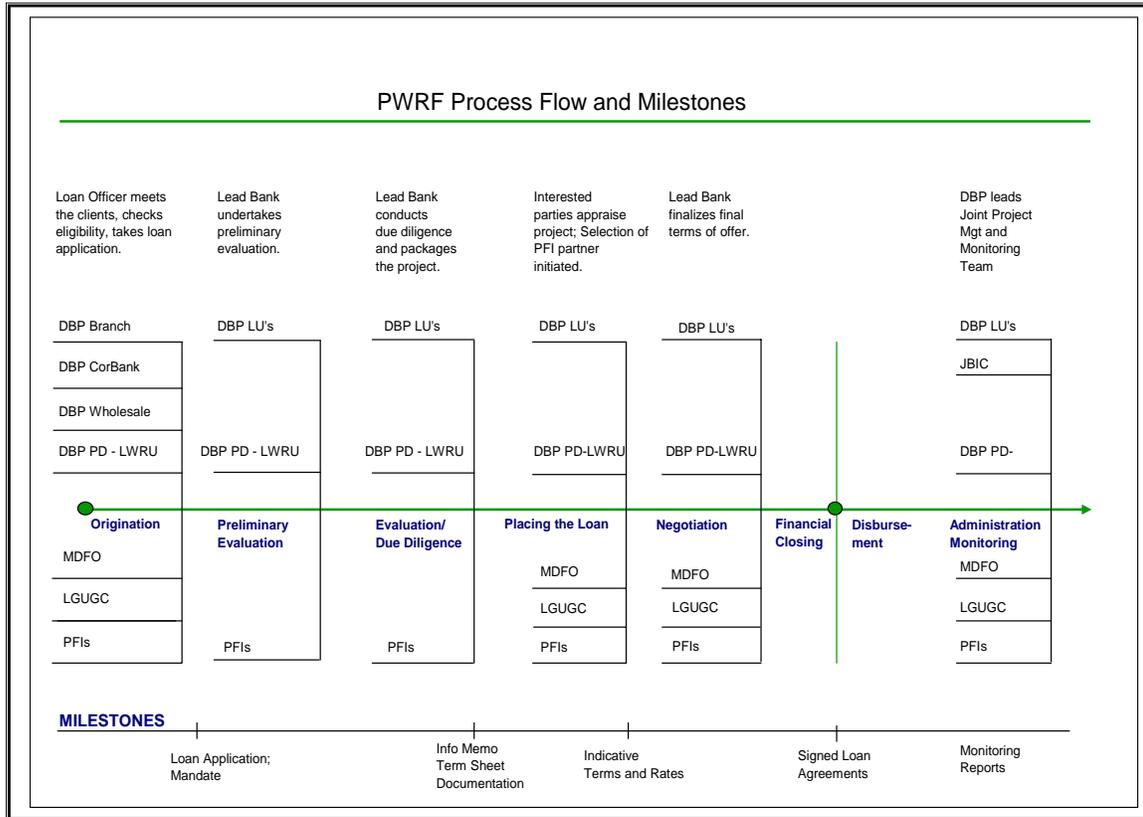
### 1.7.1 Assistance to DBP on the preparation of the PWRF business and marketing plan

We will help DBP prepare the business plan and the marketing strategy for PWRF. The business plan will provide DBP Senior Management with an action plan for DBP to perform a catalytic role in encouraging private sector participation in water lending. The assistance will cover the following:

- Assist DBP in coming up with a medium term business plan for the Land and Water Resources Unit that will identify opportunities and risks in the water and sanitation sector; and how DBP through its participation could encourage private financing institutions to lend to the sector.
- Review the Bank's performance targets with branches and recommend indicators to conform with the objectives of PWRF to encourage PFI lending
- Facilitate discussions towards making more concrete financial targets for DBP in terms of loan exposure to the water sector and PFI partners.
- Assist DBP in conceptualizing the marketing plan for PWRF including coming up with standard marketing kits and presentations to PFI's, DBP Branch Heads, LGU leaders and other stakeholders.

### 1.7.2 Training Workshop on PWRF Process Flows

The PWRF Operating Policy Guidelines will require a re-engineering of how DBP conducts its lending operations. As such, there is a need for re-orienting DBP loan officers and regional heads. In this regard, we will conduct workshops to flesh out new procedures of PWRF. For instance, the PWRF will require a step by step training to familiarize account officers with the process from loan origination, to selection of a PFI Partner up to the joint monitoring of the water project (as shown in the chart below). The workshops will be conducted in the DBP Head Office as well as in its Regional Offices.



*\*LUs refer to the Lending Units while LWRU refers to Land and Water Resources Unit of DBP.*

### 1.7.3 Continuing Updates of PWRF Operating Guidelines and Documentation

As part of our continuing effort to provide technical support in establishing the PWRF in its initial implementation phase, we will assist PWRF implementers further refine the operating policy guidelines of DBP and MDFO; and the standard loan documents, including the inter-creditor agreement. The standard loan agreements include the General Terms and Conditions, Term Loan Agreement, Deed of Assignments, Standby Loan Agreement, the Guarantee Agreement. The technical assistance will guide the PWRF partners how to standardize the loan documentation and to make the said documents consistent with the requirements for a pooled bond offering.

Relatedly, we will also continue to backstop DBP in facilitating the JBIC loan application process and complying with the requirements. One case in point, we will assist DBP establish a procurement system for technical assistance akin to USAID's indefinite quantity contracts. This will enable DBP to compete in a relatively quick and transparent manner tailor-fitted technical assistance services that may be required later.

## **Component 2: Water/Sanitation Project Development**

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### **OBJECTIVE**

Assist water districts and LGUs in improving capacity to prepare water supply and sanitation projects and institutionalize a project development facility; on demand basis, assist with the update or improvement of pre-investment studies to get them acceptable to lenders

### **COMPONENT 2 DELIVERABLES**

- On demand basis, TA to water utilities to update or upgrade pre-investment studies
- Feasibility Assessment and Design of a Project Development Facility
- Implementation guidelines for the LWUA-administered Project Development and Efficiency Improvement Fund
- Feasibility analysis of septage management in water districts and business model
- LGU training program on WSS project development

### **PLANNED ACTIVITIES**

#### **2.1 Assist Utilities to Update Feasibility Studies and Prepare Projects for PWRF Funding on Demand Basis**

The JBIC demand analysis surveyed creditworthy utilities and identified 21 candidate projects for PWRF funding with estimated costs of PhP 8.2 billion. Our rapid screening of these projects has shown that many have outdated pre-investment studies (more than three years old), and thus need updating for funding consideration.

In this regard, we initially planned to pro-actively seek out the projects for funding and targeted 4 to 7 utilities assisted with feasibility studies update or improvement. However, this approach has proven inefficient. The resources required to do the updates are quite substantial and in the end there is no guarantee that the water utilities will indeed pursue the project or that PWRF financing will be accessed.

In view thereof, we agreed with USAID to keep this task but to provide the TA on demand basis. Our team will respond to request for assistance from water utility borrowers identified by LGUGC and DBP, and who have given letters of intent to borrow from PFIs or joint PFIs and GFIs.

Our assistance can include not only update and improvement of the feasibility study but also quick interventions on operational, financial and management improvements aimed at improving the viability of the project. For instance, our team can help analyze and map out approaches to revise tariff rates to reflect full cost of operations, improve billings and collections, and recommend other changes to improve overall utility operations and financial performance.

***Special Assistance to Jolo Water District*** -Upon the request of USAID, special assistance will be provided to Jolo Water District on capacity building. The effort will be coordinated with GEM, another USAID project based in Mindanao.

## **2.2 Feasibility Assessment and Design of the Project Development Facility**

Many utilities have highlighted the lack of access to funds for project development as a key constraint to preparing projects for system expansion and upgrade. The team will use the analysis of options and recommendations completed in Year 1, and work with DOF to carry out a feasibility assessment and design of setting up a project development facility that can provide loans and grants, where needed, to utilities for project feasibility and detailed design studies.

This task will complement the task described in 2.3 below. The objective is to institutionalize a project development facility that is not tied to any lending program; can be accessed by water districts, LGUs and possibly even private water service providers; and has a revolving feature.

## **2.3 Implementation Guidelines of the LWUA-administered Project Development and Efficiency Improvement Program**

The PWRF study tour group to the US identified a number of issues that constrain investments in the sector, two of which are:

- financing deal flows are low due to lack of bankable projects; and
- LWUA has no concessional funds to lend to less than creditworthy water districts for efficiency improvement measures; the idea is to target the subsidies to less than creditworthy utilities conditioned on achieving performance targets, to implement projects that will improve their creditworthiness.

DOF's Undersecretary Paul, who led the study tour group delegation, heeded these concerns and facilitated a PhP 250 million subsidy to LWUA earmarked for feasibility studies and quick gestating investments to improve efficiency, such as NRW reduction, metering or computerization. None of the funds will be given as grants, rather will be on lent at concessional terms.

Our team has been helping LWUA prepare the implementation guidelines. The policy framework, including the lending terms, is due for presentation to the LWUA Board of Trustees in February 2008. Once the policy framework is approved, our team will prepare with LWUA staff the detailed implementation guidelines.

During implementation stage, our team will backstop DOF in monitoring the Fund's disposition.

## **2.4 Feasibility Study and Business Model for Water Districts on Septage Management**

In line with the activity to promote sanitation investments by water districts, we will support pre-investment studies of Metro-Cebu Water District (classified as *very large*) and Cabanatuan City Water District (classified as *big*) for septage management. The feasibility studies will cover investments in septage collection and treatment. For Metro Cebu Water District, our team will work with the Philippine Sanitation Alliance (PSA), another USAID project. PSA will assist MCWD with the social preparation aspect, and with the promotion and mobilization of support from concerned LGUs.

MCWD and CCWD signified interest to implement septage management and willingness to use their projects as cases in point to develop a business model for other water districts. We will use these projects as demonstration cases for promoting sanitation investments to the national and regional association of WDs. The feasibility study and business model preparation will be complemented with workshops with local water district associations for sharing knowledge and testimonials from the two water districts on the viability of investments in sanitation.

## **2.5 LGU Training on WSS Project Development**

**Training programs for LGU water utilities** - Our team will conduct training of selected LGU utilities to improve their pre-investment analysis, technical design and demand forecasting, and financial analysis for new project development; as well as training on best practices on utility management and operation.

We will coordinate with DILG and MDFO to discuss TAs for the development of regular training courses for LGUs, particularly in project development, financing and utility operations. We will explore the possibility of integrating these training courses in the regular LWUA training program. PWRF will design the training course(s) and organize the initial workshops to be conducted.

**Toolkits for LGUs** – Depending on the assessment of need, we will compile toolkits to guide the water utilities on project development and utility operation.

**Ring-fencing of LGU water utility account** – We will support one LGU to ring-fence its water utility account and develop a toolkit for dissemination to other LGUs.

## **Component 3: Water and Finance Sector Strengthening**

### **OBJECTIVES**

Help implement strategic policy and institutional reforms in the water and finance sectors that facilitate achieving the targets under Components 1 and 2.

Prepare a policy paper on how to rationalize government subsidies to achieve the development objectives of the sector

### **COMPONENT 3 DELIVERABLES**

- Policy paper on the rationalization of public resource allocation for water and sanitation projects
- Support to DOF request to BSP for financial incentives for water sector lending
- Technical assistance to DOF for the coordination of water sector reform agenda (through the water sub-committee of the Philippine Development Forum)
- Conference on regulatory reform for water supply and sanitation
- Selected water utilities trained in long-term business planning and business plans required by LWUA for tariff and/or loan application approvals

### **PLANNED ACTIVITIES**

#### **3.1. Prepare a policy paper on the rationalization of public resource allocation for water supply and sanitation projects**

In Year 1, the PWRF team analyzed the need for rationalizing credit program for the water sector, and provided specific recommendations for how the existing and future credit programs could be rationalized to shift all creditworthy utilities to market-based lending provided by GFIs and PFIs. The assistance resulted in the creation of draft operating guidelines for government's adoption.

However, a new perspective was gained from the study tour conducted in US State Revolving Funds. The federal and state governments provide interest rate subsidies to utilities on the basis of development objectives the proposed investments will achieve. A stick and carrot approach is used in driving investments. The stick is essentially the strict enforcement of environmental standards (e.g., set by the Clean Water Act) and quantity and quality standards of service, with stiff penalties for non-compliance. The carrot is the financing incentive, i.e., low financing cost brought about by leveraging public funds with very low interest rates (in some cases even zero) with funds from the domestic capital market. Allocation of the subsidy is based on clearly defined criteria anchored on development objectives, and on intended use plans submitted by utilities as a pre-requisite to the loan application.

Taking off from the lessons learned from the US study tour and from the review of EO 279's financing policy guidelines, our team will prepare a policy paper on the rationalization of public resources to best achieve the sector's long-term goal of reaching 100% service coverage, standards on quality of

service, and compliance with health and environmental standards. The recommendations will inform the design of the long-term financing mechanism that will be prepared under Component 1.

Our team will draw insights and inputs from the on-going efforts of the government to prepare a water sector roadmap and from related initiatives of other donors.

### **3.2 Support DOF to put in place financial incentives for water sector lending**

Also in Year 1, we prepared the groundwork for putting in place financial incentives for water sector lending. Specifically, we prepared for DOF a position paper addressed to the Central Bank of the Philippines to:

- Approve the inclusion of water sector lending in the eligible sectors for compliance with PD 717 or better known as the Agri-agra law. This law requires banks to set aside 25% of their loan program for agriculture, agrarian reform- related and other priority sectors of the government. Banks are penalized for non-compliance. Presently banks find it difficult to achieve their quota for agri-agra law compliance.

The position paper has been accepted by DOF and will soon be submitting it to BSP. Our team will continue to backstop DOF in the ensuing discussions with BSP to secure its approval.

Our team will also propose this incentive: allow water financing instruments as eligible securities to comply with the BSP reserve requirements for deposits.

Both were cited by private financing institutions as powerful incentives. The LWUA securitization transaction will be used as the live case to advocate for these incentives with BSP.

### **3.3 Technical assistance to DOF for the coordination of water sector reform agenda (through the water sub-committee of the Philippine Development Forum)**

DOF requested technical assistance from USAID to help it coordinate the overall reform agenda for the sector. In particular, DOF requests technical secretariat support for the sub-committee on water that will be established under the Philippine Development Forum. The sub-committee will have representation from GOP, donors and private sector, and will serve as the venue to discuss issues and get consensus on the reform agenda and related action plan for the sector.

DOF has taken up the challenge of ensuring the comprehensiveness and coherence of the reform agenda, realizing that for financing reforms to be effective, parallel regulatory and institutional reforms should be in place.

USAID approved the request and will provide the TA through the PWRF-SP. Our team will thus assist DOF in preparing the charter of the sub-committee and propose its overall agenda. We will also assist DOF with the preparation of discussion/analysis papers and recommendations, where our team has core expertise. To help with the facilitation of the TA with DOF, we will assign a consultant to work directly with the office of Undersecretary Jeremias Paul.

### **3.4 Conference on regulatory reform for water supply and sanitation**

Related to the efforts described in 3.3 above, our team will organize a conference on regulatory reform for water supply and sanitation. Strengthening of regulations is deemed as one if not the most critical piece of the reform agenda. It could be the linchpin for utility and financing reforms. However, important as it may be, it would not be efficient use of PWRF-SP resources to dabble in the regulatory reform measures. Instead, PWRF-SP will sponsor a forum among concerned GOP officials, key stakeholders and international experts to discuss the regulatory reform program. International experts will be invited to share lessons from other countries' experiences and their insights on the program.

### **3.5 Assist Water Utilities in Preparing Business Plans**

Our team will assist selected WDs and LGUs in their long term planning and investment programming. In this regard our team prepared a business plan framework under the Year 1 work plan. This framework was submitted to LWUA for its comments, and LWUA agreed on the scope. Under the Year 2 work plan, we will prepare training modules, and a business plan guidebook. We will then conduct at least three regional business planning workshops. We will follow this up with advisory support to water districts or LGUs who prepare their business plans after the workshops.

We will also propose to LWUA to adopt the training design and modules and offer the course in its regular training program. In addition, we will also propose to make the business plan a requirement for the loan and/or tariff adjustment application of water districts. This way we hope to motivate water districts to adopt business planning as a good governance tool.

## **Component 4: General PWRF Program Support**

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### **OBJECTIVE**

Provide technical secretariat support to the PWRF Steering Committee and Technical Working Group; and support USAID in reporting, advocacy and collaboration with JBIC on the PWRF.

### **COMPONENT 4 DELIVERABLES**

- At least one meeting per quarter for the Steering Committee and the Technical Working Group
- Meetings and consultations scheduled as necessary with the key implementers
- Technical papers, presentations, inputs to USAID reports and communication materials on the PWRF, as may be required by USAID
- Set up and maintain PWRF Support Program Website

### **PLANNED ACTIVITIES**

#### **4.1 Provide technical secretariat support to the PWRF Steering Committee and Technical Working Group**

We will continue to provide technical secretariat support to the PWRF Steering Committee and its Technical Working Group. We will also continue to provide technical support to key implementers as necessary. We will facilitate policy and operational decisions by preparing thorough analyses of issues for resolution.

#### **4.2 Provide Support to USAID's Reporting, Advocacy and Collaboration with JBIC on the PWRF**

We will support USAID's collaboration with JBIC on the PWRF by hosting meetings, carrying out any required analyses, and producing reports and other communications materials. We will respond to any request of USAID to provide inputs to its reporting and advocacy needs for the PWRF program. We can also provide technical and logistic support to any workshop or forum that USAID and JBIC may organize to promote their collaboration. Our team can also serve as a resource group for similar initiatives of USAID and JBIC in other target countries, e.g., Indonesia.

#### **4.3 Knowledge/Information Dissemination and Management**

The team will design a PWRF website that can serve as a portal for reports and other information related to the PWRF, and also provide access for stakeholders to other information related to water sector finance, revolving funds and water utility operations. While the PWRF website will initially be managed by the team, we anticipate moving the website management and maintenance to the PWRF unit to be established within DBP.

## Opportunities for Collaboration with USAID and Other Donor Projects

The team recognizes the opportunities for synergy with USAID and other related donor projects, through complementation of efforts, reinforcement of common objectives and advocacy for reforms with key partners. Presently, we will work closely with the following USAID projects:

### Philippine Environmental Governance Project 2 (EcoGov2)

We will coordinate with EcoGov in the areas of promotion of sanitation investments among water districts; assistance to LGUs and WDs in developing business plans for sanitation and in identifying financing options for sanitation projects.

### Environmental Cooperation Asia (EcoAsia)

The project is assisting the Local Water Utilities Administration design financial products for its new market, the semi- and pre-creditworthy water utilities. The products will focus on financing efficiency improvements that will improve the creditworthiness of these utilities. This initiative directly complements the PWRF as it caters to long-term financing needs of creditworthy utilities. EcoAsia's strategic support toward graduating water utilities to becoming creditworthy will help broaden the market for PWRF or facilitate the shift of the sector's financing to market-based sources. Areas of collaboration could include complementary support to EO 279 Oversight Committee on rationalization of credit programs and ensuring alignment of LWUA policy with EO 279. In particular, EcoAsia's approach will address the moral hazard of providing concessional funds to less than creditworthy utilities.

Moreover, regulatory reform being a shared interest with EcoAsia, we will collaborate with them in the organization of the conference on regulatory reform described under Component 3. In particular, EcoAsia may be able to identify and provide one of the international experts as well as share any materials that they have on the experience of other countries.

If it wishes to, EcoAsia can send representatives from its partners who may benefit from the conference.

### Water and Sanitation Program (WSP)

WSP has signified its interest to focus its assistance on regulatory reform. We plan to consult with them on the conference program and to exchange information or resources on regulatory reform.

### World Bank TA Program to LWUA

World Bank is undertaking technical assistance project to LWUA. The TA has five components, namely:

#### Box 2. EcoGov2's TA Products for Waste Water Management

- Advocacy/IEC on health benefits of WWM
- Rapid WWM needs assessment approach and tools
- WWM technical design options
- WW user fees
- Developing and implementing WWM ordinances
- Facility management
- Monitoring and evaluation of WWM services

- Clustering of water utilities under one management structure
- Incentives to LWUA related to the implementation of EO 279
- Impact of EO 279 lending policy to LWUA's financial position
- Stakeholders' Survey on LWUA's Services
- Role of Private Water Service Providers

Our team will coordinate closely with the WB TA team to ensure exchange of information and coordination of recommendations on policy measures.

**GTZ's Water Supply Road Map (with NEDA as the GOP counterpart for the study)**

GTZ has supported the preparation of an institutional framework for water supply development. The next step after government's acceptance of the recommendations will be the preparation of a development road map, which would include financing, regulatory reform, capacity building of utilities and oversight agencies, and improving governance and overall performance of utilities. We will coordinate with the study team to determine in which policy areas we can support each other.

**Figure 1: PWRF Year 2 Work Plan**

MAJOR TASKS	Phase 1: Year 2												Responsibility (L=Lead)	Expected Outputs/ Status	
	Oct 07	Nov 07	Dec 07	Jan 08	Feb 08	Mar 08	Apr 08	May 08	Jun 08	Jul 08	Aug 08	Sep 08			
<b>Component 1: PWRF Set-Up and Institutional Development</b>															
<b>1.1 Assist USAID Philippine Mission prepare the guarantee agreement between DCA and LGUGC</b>															
Prepare inputs to the Action Memo for DCA approval of the guarantee agreement														Porciuncula (L)+ Team	Draft Action Memo
Backstop Mission and DCA in the negotiation														Porciuncula (L)+ Team	As may be required by USAID
<b>1.2 Assist LWUA with securitization of its receivables</b>															
Initiate discussion with LWUA on undertaking securitization of its receivables														Porciuncula, Pantillano and Saulog	MOU with LWUA on TA for securitization
Assist LWUA management with approvals for securitization														Porciuncula, Pantillano and STTA (Lawyer)	LWUA Board approval of MOU
Provide TA to LWUA on securitization process														Pantillano (L) + STTAs	Advisory Assistance for the securitization plan and technical implementation support; LWUA securitization guideline
<b>1.3 Assist Water District/s with a Bond Transaction</b>															
Identify potential project with water districts														Asuncion (L)+ Team	List of potential project for bond financing
Orient water district/s with bond transaction and confirm interest, and get approval for a bond issue														Porciuncula + Pantillano	Orientation of WDs and getting expressions of interest for bond financing
If interested assist WD with structuring of the bond issue														Pantillano (L)+ STTA	Financial advisory assistance
<b>1.4 Prepare roadmap for long term financing structure of PWRF</b>															
Following the financing policy framework in 3.1, prepare the design and implementation plan of PWRF's long term financing mechanism														Pantillano (L)+ Brad Johnson + STTA	Design of Long-term financing mechanism
Assess acceptability and demand														Pantillano (L)+ STTAs	Demand Analysis

MAJOR TASKS	Phase 1: Year 2											Responsibility (L=Lead)	Expected Outputs/ Status		
	Oct 07	Nov 07	Dec 07	Jan 08	Feb 08	Mar 08	Apr 08	May 08	Jun 08	Jul 08	Aug 08			Sep 08	
Conduct policy consultations on the financing structure														Pantillano (L)+ STTAs	Key Informant Interviews and Focused Group Discussions
Prepare implementation guidelines														Pantillano (L)+ Brad Johnson+ STTA	Implementation guidelines for long term financing mechanism
<b>1.5 Train PFIs and other PWRF Stakeholders on Water Project Appraisals and conduct DBP RMC Briefings on PWRF</b>														Pantillano(L)/ Asuncion +STTA	Training on Project Appraisal (3 regional workshops)
<b>1.6 Prepare Water Project Appraisal Guidebook for Lenders</b>															Water Project Appraisal Guidebook
Draft Project Appraisal Guidebook														Pantillano (L)/Asuncion/ Porciuncula+STTA	Draft Guidebook
Edit and Print														Pantillano (L)/ Porciuncula + STTA	
Launch Guidebook														Pantillano (L)/Mendoza	Water Project Appraisal Guidebook
<b>1.7 Provide institutional support to DBP to establish PWRF lending window (subject to JBIC loan commitment)</b>															
Assist DBP prepare a medium term business plan for PWRF														Pantillano(L)/ Porciuncula +STTA	Medium Term Business Plan for PWRF (contingent on JBIC EDP Loan pledging)
Assist DBP Prepare PWRF Marketing Materials														Pantillano (L)/ Porciuncula +STTA	PWRF Marketing Materials (contingent on JBIC EDP Loan pledging)
Assist DBP in the implementation of the marketing plan														Pantillano (L)/ Porciuncula +STTA	Inputs on Marketing Plan Implementation (contingent on JBIC EDP Loan pledging)
Conduct training on Loan Packaging and Syndication														Pantillano (L)/ Porciuncula +STTA	Training Workshop on Loan Packaging and Syndication (3 regional workshops)
Train DBP staff on PWRF Operating Policy Guidelines														Pantillano (L)+ Porciuncula + STTA	Training Workshop on PWRF Operating Guidelines and Process Flows (3 regional workshops)
Prepare IQC Procurement System for TA Component														Porciuncula (L) + Pantillano and Asuncion	Procurement system for pre-investment studies

**Component 2: Water and Sanitation Project Preparation**

**2.1 Assist utilities to update feasibility studies and finalize projects for PWRF funding**

MAJOR TASKS	Phase 1: Year 2												Responsibility (L=Lead)	Expected Outputs/ Status	
	Oct 07	Nov 07	Dec 07	Jan 08	Feb 08	Mar 08	Apr 08	May 08	Jun 08	Jul 08	Aug 08	Sep 08			
On demand basis, evaluate level of preparedness of project feasibility studies; or assist targeted utilities improve project feasibility studies, for financing from the PWRF; or assist LGUGC and DBP evaluate projects for financing														Asuncion (L)/Pantillano+ STTA	Projects ready for financing, including LGUGC projects with PFI and LWUA co-financing
As a special case, requested by USAID, assist Jolo Water District with capacity building														Asuncion (L), Pantillano + STTA	Assessment of improvement measures and TA on business planning
<b>2.2 Conduct Feasibility Assessment of the Project Development Facility</b>															
Prepare Concept, demand analysis, design and implementation plan for a PDF														Porciuncula (L) + Asuncion, McCluskey	Design and Implementation Plan for a Project Development Facility
<b>2.3 Assist LWUA prepare Implementation guidelines for the LWUA-administered Project Development and Efficiency Improvement Fund</b>															
Prepare policy framework for implementation guidelines														Asuncion (L)+ Pantillano+ Porciuncula	LWUA Board approval of framework
Assist LWUA prepare the operating guidelines														Asuncion (L)+ Pantillano+ Porciuncula	PDEIF Operating Guidelines
Prepare model RFPs and tender documents for bulk water supply														Asuncion(L) + STTA	Model RFPs/Tender Documents for Bulk Water Supply
<b>2.4 Promote sanitation system development by water districts</b>															
Prepare Feasibility Study for Septage Management for MCWD and CCWD Business Model for WDs														Asuncion (L)+ STTAs	FS for Metro Cebu WD and Cabanatuan City WD for a septage management project and business model for WDs
Conduct workshops to disseminate business model														Asuncion (L) + STTAs	3 regional workshops with local association of WDs
<b>2.5 Design and conduct training course for LGUs for project development, financing, and utility operations – LWUA and DILG</b>															
Assess training needs in consultation with DILG														Asuncion (L) + STTAs	TNA report
Prepare course design														Asuncion (L)+ STTAs	Course design report

MAJOR TASKS	Phase 1: Year 2												Responsibility (L=Lead)	Expected Outputs/ Status		
	Oct 07	Nov 07	Dec 07	Jan 08	Feb 08	Mar 08	Apr 08	May 08	Jun 08	Jul 08	Aug 08	Sep 08				
Conduct pilot training and institutionalize training program in LWUA														Asuncion (L) +STTAs	2 training seminars; institutionalization arrangement between LWUA and DILG	
<b>Component 3: Water and Finance Sector Strengthening</b>																
<b>3.1 Prepare policy paper on the rationalization of public resource allocation for water supply and sanitation projects</b>																
Prepare policy paper															Policy Specialist (TBD)	Policy Paper on rationalization of public resource allocation for WSS
<b>3.2 Support DOF put in place financial incentives for water sector lending</b>																
Provide technical support to DOF in securing BSP approval of agri-agra eligibility of water sector lending															Navarro, Porciuncula	Technical support to DOF
Provide technical support to DOF in securing BSP approval of allowing water financing instruments as eligible securities to comply with reserve requirements.															Policy Specialist (TBD)	Technical support to DOF
<b>3.3 Assistance to Philippine Development Forum (contribution to the water sector reform agenda)</b>																
Provide technical secretariat support to the PDF sub-committee for water															Porciuncula (L)+ Team	Financing Policy Framework
Backstop DOF in the water sector subcommittee of the PDF on the coordination of the sector's reform agenda															Policy Specialist (L)+ Team + PWRF Staff support to Usec Paul	Technical Support to DOF
<b>3.4 Conference on regulatory reform for water supply and sanitation</b>																
Plan and organize conference on regulatory reform															Porciuncula (L) + de Vera+ Mendoza	Conference design, program and discussion paper
Conduct conference															Facilitator (TBD)+ NWRB+ International Experts	Conference and proceedings
<b>3.5 Prepare business planning framework for utilities</b>																
Prepare training modules/toolkit on business planning for WDs and LGUs															Asuncion (L)+ Team+ STTA	Training modules/toolkit

MAJOR TASKS	Phase 1: Year 2											Responsibility (L=Lead)	Expected Outputs/ Status	
	O c t 0 7	Nov 07	Dec 07	Jan 08	Feb 08	Mar 08	Apr 08	May 08	Jun 08	Jul 08	Aug 08			Sep 08
Conduct training on business planning among selected participants													Asuncion (L) + Team+ STTA	Training on business planning
Provide advisory assistance to selected utilities in the preparation of their business plans													Asuncion (L)+Team + STTA	Advisory assistance to utilities preparing business plans
Facilitate institutionalization of business planning among utilities													Asuncion (L)+ Team	Agreement with LWUA to require a business plan for tariff adjustment applications
<b>Component 4: General PWRF Program Support</b>														
<b>4.1 Provide technical secretariat support to the PWRF Steering Committee, the Technical Working Group, and the Working Group that will be convened as a result of the MOU for Implementation</b>													Porciuncula (L)+ Team	Technical secretariat support to PWRF Committees
<b>4.2 Provide overall support to USAID's reporting, advocacy, and collaboration with JBIC on the PWRF</b>													Porciuncula(L)+ Team	Overall program support to USAID and to the USAID/JBIC collaboration
<b>4.3 Maintain PWRF Website</b>													Mendoza (L) + Team	PWRF Website
<b>4.4 Prepare and maintain PWRF PMP</b>													Porciuncula (L), Mendoza + Team	PWRF PMP

## Budget

### STATUS OF THE BASE PERIOD BUDGET

	BUDGET	CUMULATIVE EXPENDITURES (as of Dec 07)	REMAINING (as of Dec 07)
<b>Labor</b>	160,498	136,385	24,113
<b>Other Direct Cost (Inclusive of Transportation and Program Activities)</b>	268,320	180,637	87,683
<b>Subcontracts</b>	329,852	193,167	136,685
<b>Indirect Costs (Fringe Benefits, Overhead &amp; G&amp;A)</b>	144,655	117,332	27,323
<b>SUBTOTAL</b>	903,325	627,521	275,804
<b>Fixed Fee</b>	59,761	43,731	16,030
<b>Grants</b>	0	0	0
<b>TOTAL (Obligated Fund)</b>	<b>\$963,086</b>	<b>\$671,252</b>	<b>\$291,834</b>
<b>PERCENT BUDGET EXPENDED</b>			<b>69.70%</b>

### PROPOSED BUDGET REALIGNMENT FOR OPTION PERIOD YEAR 2

	(A) BUDGET Year 2	(B) Proposed Realignment	(C) CUMULATIVE EXPENDITURES (as of Dec 2007)	(B-C) REMAINING AMOUNT
<b>Labor</b>	284,833	378,120	17,503	360,617
<b>Travel, Transportation &amp; Per Diem</b>	54,888	93,239	25,225	68,014
<b>Other Direct Cost</b>	89,405	82,214	1,840	80,374
<b>Program Activities</b>	124,660	225,503	2,553	222,950
<b>Subcontracts</b>	303,151	404,648	4,659	399,989
<b>Indirect Costs (Fringe Benefits, Overhead &amp; G&amp;A)</b>	198,090	191,870	7,958	183,912
<b>SUBTOTAL</b>	1,055,027	1,375,594	59,738	1,315,856
<b>Fixed Fee</b>	70,093	91,360.48	2,006	68,087
<b>Grants</b>	50,000	0	0	0
<b>TOTAL</b>	<b>\$1,175,120</b>	<b>\$1,466,954</b>	<b>\$61,744</b>	<b>\$1,383,943</b>
<b>TOTAL (Obligated Fund)</b>	<b>\$1,036,914</b>			
<b>PERCENT BUDGET EXPENDED</b>				<b>5.95%</b>

\*1 The proposed budget for Year 2 is explained as follows:

Allocation - Year 2	\$1,175,120
Add: Remainder - Year 1	\$291,834
<b>Total Proposed Budget - Year 2</b>	<b>\$ 1,466,954</b>

**SUMMARY OF LIFE OF PROJECT BUDGET  
 2006 - 2011**

	BUDGET Year 1	BUDGET Year 2	BUDGET Year 3	BUDGET Year 4	BUDGET Year 5	TOTAL
Labor	136,385	378,120	262,894	259,217	231,134	1,267,750
Travel, Transportation & Per Diem	61,741	93,239	53,988	48,744	42,003	299,715
Other Direct Cost	97,507	82,214	91,516	83,413	83,545	438,195
Program Activities	21,389	225,503	53,796	36,041	25,758	362,487
Subcontracts	193,167	404,648	397,678	189,523	204,313	1,389,329
Indirect Costs (Fringe Benefits, Overhead & G&A)	117,332	191,870	189,242	171,428	161,716	831,588
<b>SUBTOTAL</b>	<b>627,521</b>	<b>1,375,594</b>	<b>1,049,114</b>	<b>788,366</b>	<b>748,469</b>	<b>4,589,064</b>
Fixed Fee	43,731	91,360	69,333	52,503	49,752	306,679
Grants	0	0	50,000	50,000	0	100,000
<b>SUBTOTAL Yr-1</b>	<b>\$671,252</b>					
<b>Remainder Yr-1</b>	<b>\$291,834</b>					
<b>TOTAL</b>	<b>\$963,086</b>	<b>\$1,466,954</b>	<b>\$1,168,447</b>	<b>\$890,869</b>	<b>\$798,221</b>	<b>\$4,995,743</b>

## Annex 1

### Summary of Agreements PWRf Work Plan Workshop Vista Marina, Subic Bay Freeport Zone ♦ 11-12 February 2008

#### Participants

PWRf Team	USAID
1. Alma Porciuncula	7. Daniel Moore
2. Del McCluskey	8. Joy Jochico
3. Rodolfo Pantillano	
4. Ferdinand Asuncion	
5. Aida Mendoza	
6. Liza Cruz	

#### Program

1. Statement of USAID objectives for the Program	Daniel Moore
2. Taking stock of the PWRf initiative	Joy Jochico
3. Review of accomplishments	PWRf Team
4. Re-strategizing PWRf and key result areas/ priority activities	Group discussion
5. Contract Modifications	Alma Porciuncula

#### Summary of Agreements

Notwithstanding the delay of the JBIC loan and changes in the operating environment of PWRf, USAID stated that the PWRf initiative is still a relevant and an effective financing reform instrument. However, there has to be adjustments in the approach and prioritization of activities to adapt to new constraints as well as to capitalize on the emerging opportunities in the market, and to factor in lessons learned and insights from the US study tour on state revolving funds.

**Strategic adjustment-** The key lessons learned from the US study tour are i) government subsidies for water and sanitation projects is given in the form of interest rate subsidies, and not as outright capital dole-outs; ii) federal and state grants are used to leverage capital market resources; iii) the allocation of interest rate subsidies is based on the development objectives, primarily on the compliance of utilities to environmental standards; and iii) the provision of concessional loans is the “carrot” or the counterpoint to the “stick”, which is the strict enforcement of environmental and quality of service regulations.

This presented a new perspective on the rationalization guidelines of EO 279, which is focused on the creditworthiness of utilities, i.e., creditworthy utilities should not be eligible for subsidies. This has been the premise of the design for PWRf. The group agreed to review the rationalization guidelines and present a new framework to DOF, which will then be the basis for the design of the long-term mechanism for PWRf. The new framework will be presented through a policy paper (to be submitted to Usec Paul) reviewing the government subsidy to the water sector, and the economic analysis of why allocation should be on the basis of development objectives and not merely on the creditworthiness of utilities. The paper should also include analysis on who should provide the subsidy, how much is the necessary subsidy to the sector, where to get it, and in what form it will be provided. The paper is envisioned to lead to an amendment of the EO 279’s policy guidelines for public resource allocation.

The group also recognized the critical need for drivers for utilities to invest to meet performance and environmental standards. The financing incentive as seen in the case of the US is important but has to be coupled with enforcement of regulations. However, PWRf-SP does not have adequate resources to tackle regulatory and corollary institutional reforms in a significant way. Hence, it was agreed to support this undertaking by sponsoring a conference to discuss and agree on the priority measures and action plan for regulatory reform, and by providing technical assistance to DOF in the coordination the water sector reform agenda through the sub-committee for water under the Philippine Development Forum.

**Tactical changes and updates** – The following changes were agreed:

- In view of the delay of the JBIC loan, re-focus component 1 to testing capital market instruments such as the LWUA securitization and possibly bond issuance if there is any interested water district or LGU; and formulation of the long-term financing framework for PWRf based on the recommendations on public resource allocation
- Keep a place holder for institutional support to DBP in case the JBIC loan is pledged within Year 2
- The technical assistance to water districts or LGUs for project development will be on demand basis, i.e., LGUGC or DBP may request PWRf-SP’s assistance for projects already being considered for financing
- Upon the request of USAID, special assistance on management improvements will be provided to Jolo Water District to complement USAID’s capital grant thereto
- In lieu of inputs to the National Sewerage and Septage Management Plan, support two feasibility studies on septage management for a very large and big water district, and use these to prepare a business model and as demonstration cases for other WDs

The group then agreed on the following **expected outputs** for the Year 2 work plan:

<b>Component 1</b>	<ul style="list-style-type: none"> <li>▪ Action Memo to DCA requesting approval of its Credit Review Board on the new guarantee agreement with LGUGC</li> <li>▪ TA to LWUA for the securitization of its receivables</li> <li>▪ On demand basis, TA to a water district for a bond issuance</li> <li>▪ Concept and Design of a long-term financing mechanism (informed by the result of the policy analysis on resource allocation)</li> <li>▪ Training Workshops for PFIs and PWRf Partners on Water Project Appraisal</li> <li>▪ Water Project Appraisal Guidebook for Lenders</li> <li>▪ Subject to JBIC loan commitment, institutional support to DBP establish PWRf lending window</li> </ul>
<b>Component 2</b>	<ul style="list-style-type: none"> <li>▪ On demand basis, TA to water utilities update or upgrade pre-investment studies</li> <li>▪ Feasibility Assessment and Design of a Project Development Facility</li> <li>▪ Implementation guidelines for the LWUA-administered Project Development and Efficiency Improvement Fund</li> <li>▪ Feasibility analysis of septage management and preparation of a business model for water districts</li> <li>▪ LGU training program on WSS project development</li> </ul>

<b>Component 3</b>	<ul style="list-style-type: none"> <li>▪ Policy analysis on the rationalization of public resources for water supply and sanitation investments</li> <li>▪ Financial incentives for WSS lending</li> <li>▪ Technical support to DOF for its leadership in the sub-committee for water under the Philippine Development Forum</li> <li>▪ Conference on regulatory reform for water supply and sanitation</li> <li>▪ Training and institutionalization of business planning among water utilities</li> </ul>
<b>Component 4</b>	<ul style="list-style-type: none"> <li>▪ Overall program support to USAID and its collaboration with JBIC</li> <li>▪ Technical secretariat support to the PWRF Steering Committee</li> <li>▪ Knowledge management tool: PWRF website</li> </ul>

On the discussion of ***contract modifications***, the COP discussed with the CTO the re-alignment of the remainder of the Year 1 to the Year 2 budget; relatedly, carry over the pending deliverables of Year 1 to the Year 2 work plan.