



Technical Assistance Report

Project Number: 38275
December 2005

Proposed Technical Assistance Republic of the Philippines: Local Governance and Fiscal Management Project

CURRENCY EQUIVALENTS

as of 6 March 2006

Currency Unit	–	peso (P)
P1.00	=	\$0.0195
\$1.00	=	P51.17

ABBREVIATIONS

ADB	–	Asian Development Bank
CSC	–	Civil Service Commission
CMT	–	Change Management Team
DBM	–	Department of Budget and Management
DOF	–	Department of Finance
DILG	–	Department of Interior and Local Government
e-LGAS	–	electronic local government accounting system
GOCC	–	government owned and controlled corporation
ICT	–	information and communication technology
IRA	–	internal revenue allotment
LGU	–	local government unit
LGC	–	Local Government Code of 1991
LGUGC	–	Local Government Unit Guarantee Corporation
NCR	–	National Capital Region
NEDA	–	National Economic and Development Authority
NGA	–	national government agency
SIE	–	Statement of income and expenditures
TA	–	technical assistance

TECHNICAL ASSISTANCE CLASSIFICATION

Targeting Classification	–	General intervention
Sector	–	Law, Economic Management and Public Policy
Subsector	–	Subnational government administration, Public finance and expenditure management
Themes	–	Sustainable economic growth, governance, and capacity development, Promoting macroeconomic stability
Subthemes	–	Public governance, Institutional development

GLOSSARY

barangay – A village within a city or municipality.

NOTES

- (i) The fiscal year (FY) of the Government ends on 31 December.
- (ii) In this report, "\$" refers to US dollars.

Vice President	C.L. Greenwood, Jr., Operations Group 2
Director General	S. R. Curry, Officer-in-Charge
Team leader	W. Bikales, Principal Economist, SERD
Team member	E. L. Araneta, formerly Senior Governance Specialist, SERD

I. INTRODUCTION

1. The Government of the Republic of the Philippines (the Government) requested the Asian Development Bank (ADB) to provide advisory technical assistance (TA)¹ for local governance and fiscal management. The TA is included in the Country Strategy and Program 2005-2007 for the Philippines. Fact finding was conducted intermittently from July to August, after which a memorandum of understanding was signed confirming the objective, scope, cost estimates, financing, and implementation arrangements of the TA. The TA design and monitoring framework is in Appendix 1.

II. ISSUES

2. The Local Government Code of 1991 (LGC) was an ambitious effort to transform local government units (LGUs) from mere agents of the national Government into autonomous managers of the design, funding, and delivery of key government services at the local level. For each level of LGU² a clear mandate and sphere of administrative and financial autonomy were defined. The share of Government domestic revenues transferred to LGUs was doubled to 40%,³ and LGUs were empowered to create their own revenue sources such as levies, taxes, fees, and charges, and to access credit markets.

3. Fourteen years later, the LGU share of government operations has more than doubled, and decentralization is a reality in the Philippines. At the same time, the Government and people are acutely aware that the ambitious vision of effective and autonomous local governance has been only partly realized. Devolution of expenditure authority to LGUs has been complicated by ambiguities and contradictions in expenditure assignments between national Government agencies (NGAs) and LGUs. LGU resource mobilization has frequently proven inadequate, leading to heavy dependence on transfers from the national budget and insufficient resources for essential infrastructure investment. LGU tax administration, budgeting, and financial management processes are in many cases not up to the requirements of a decentralized system. NGAs have not made some necessary adjustments to the changed demands created by more autonomous LGUs and lack some of the necessary structures, procedures, and information systems to exercise their reformed oversight roles in local government activities. Effective local governance is hindered by the weak legal and institutional framework for decentralization, as well as by capacity constraints both locally and nationally.

4. Inadequate LGU resource mobilization is a critical constraint. Cities and wealthier municipalities are often unable to take advantage of their economic strength to access financial markets to finance investment projects. Mid-level (level 3 and 4)⁴ municipalities need to build creditworthiness to be able to access credit markets and also need to strengthen tax collections, particularly the real property tax and business tax. Poorer LGUs require improvements in lending and ongranting practices for Government and donor funds, and strengthened tax collection capacity. It is also necessary to prepare adjustments in the internal revenue allotment (IRA), the main intergovernmental fiscal transfer instrument, in which the allocation formula does not consider the fiscal capacity of the LGU, so that LGUs with similar populations and land areas receive the same amount, even if their economic conditions are vastly different. Creating

¹ The TA first appeared in *ADB Business Opportunities* (internet edition) on 13 July 2005.

² There are three levels of LGUs, (i) directly below the national Government are provinces and certain cities designated as "highly urbanized," (ii) under provincial supervision are component cities and municipalities; and (iii) barangays, which are villages within a city or municipality and have very limited governing powers.

³ That is, 40% of domestic revenues from 3 years earlier.

⁴ The Government classifies all LGUs into six income levels, with Level 1 the highest and Level 6 the lowest income.

an additional performance-based transfer mechanism will also help correct current poor incentives for IRA-dependent LGUs, as many LGUs that receive large transfers choose to avoid the political costs of tougher tax collection.⁵

5. Weak LGU expenditure management also limits the effectiveness of local governance. Shortcomings include (i) excessive personnel expenses, crowding out spending on services and investment; (ii) the lack of long-term revenue and expenditure estimation capacity, weakening investment planning; (iii) undeveloped internal financial audit capacity; and (iv) opaque budget formulation and execution practices.

6. A number of important new Government initiatives are being taken to strengthen LGU administration and fiscal management. The Government issued Executive Order 444 in July 2005, directing the Department of Interior and Local Government (DILG) to identify activities of NGAs and government corporations that should be devolved. A new electronic local government accounting system (e-LGAS) is being rolled out to LGUs. The Bureau of Local Government Finance in the Department of Finance (DOF) is implementing a revised LGU financial reporting statement, the Statement of Income and Expenditures (SIE), to improve and standardize the presentation of LGU budget numbers. Initiatives are also underway to align the financial reports produced under the LGAS with the SIEs. DILG is also rolling out its new Local Government Performance Measurement System, which focuses on indicators of service delivery and provides essential information on assessing overall performance. The implementation of these vital initiatives now needs to be carefully managed and supported.

7. The donor community has actively supported improved local governance, financial management, and service delivery. ADB has extensive experience in this area. In 2003, ADB and the World Bank conducted a joint study on decentralized service delivery, which is a valuable source of information on issues relevant to this TA. The two latest ADB TA projects were approved in December 2004. TA for Strengthening Provincial and Local Planning and Expenditure Management⁶ will help establish efficient frameworks for provincial and other LGU planning processes. TA for Local Government Finance and Budget Reform⁷ will strengthen the capacity of three key national government agencies that support or directly finance LGU budgeting: the Bureau of Local Government Finance, Municipal Finance Corporation, and Local Government Academy of DILG. Other donors, including the World Bank, Canadian International Development Agency, Australian Agency for International Development and others, are active in LGUs as well. ADB coordinates closely with them through the recently established Government-Development Partners Working Group on Decentralization and Local Government, created during the 2005 Philippines Development Forum.

III. THE PROPOSED TECHNICAL ASSISTANCE

A. Impact and Outcome

8. The purpose of the TA is to support the Government's fiscal consolidation and poverty reduction agendas by improving resource mobilization, expenditure management, and public service delivery in LGUs, the front line of government social service provision, at which over 20% of total government spending takes place. By developing LGU capacity to operate more

⁵ See ADB and World Bank. 2005. *Decentralization in the Philippines*. Manila.

⁶ ADB. 2004: *Strengthening Provincial/Local Planning and Expenditure Management*, Manila, (TA 4512).

⁷ ADB. 2004: *Local Government Finance and Budget Reform Project*. Manila (TA 4556).

efficiently and effectively, these activities will contribute to improved local welfare without requiring additional Government transfers. The key outcomes of the TA will be:

- (i) enhanced LGU access to budget resources, from traditional sources such as taxes and fees, and from other sources including bank credit, bonds, and build-operate-transfer arrangements;
- (ii) improved LGU expenditure and financial management, leading to more effective service delivery and infrastructure development;
- (iii) improvements in the legal framework for decentralization; and
- (iv) an in-depth assessment of Philippine decentralization to date, with recommendations for new reform measures, including LGC revisions.

B. Methodology and Key Activities

9. The TA will support LGUs in developing sound and transparent fiscal frameworks that will serve as a foundation for strengthened budgeting and access to credit markets. The TA comprises an integrated package of activities that will address three key aspects of LGU fiscal management: (i) an improved legal framework for decentralization; (ii) transparency and effectiveness in LGU expenditure management and budget processes; and (iii) LGU capacity to mobilize sufficient resources to finance necessary services to their constituents. These three components of the work will proceed simultaneously and flexibly, with consulting assignments, workshops and other activities planned to achieve maximum impact in all three areas.

10. Improved fiscal management and service delivery will be supported in a select group of provinces and in cities and municipalities within those provinces. Around 3 provinces with component LGUs will be selected for participation, based on criteria to be developed by the TA. Participating provinces will include LGUs that have clear prospects for accessing credit markets. Some level 4-6 LGUs that have demonstrated commitment to improved governance will also be included. Other criteria will include proximity to other potential recipients of assistance in later TA phases and willingness to mentor them. Work with the LGU Leagues⁸ and NGAs will draw on this experience to provide templates and examples that can assist other LGUs.

11. **Component A:** This will support a clearer and more effective legal framework for decentralization, through the following activities:

- (i) an in-depth study of the results to date of the Philippine decentralization process, with recommendations for amendments to the LGC and other laws;
- (ii) support for accelerated devolution in accordance with Executive Order 444;
- (iii) capacity development activities for DILG and other NGAs overseeing the decentralized LGUs, including reliable and timely data on LGU performance;
- (iv) the assessment of subnational intergovernmental fiscal relations, specifically flows from provinces to municipalities and barangays, with the development of proposals for improving the relevant laws and regulations;
- (v) assessment of the impact of the current IRA formula and procedures on revenue adequacy, predictability, and collection incentives in participating LGUs, and the development of proposals for IRA reform; and

⁸ The League of Provinces, League of Cities and League of Municipalities are NGOs that were established following the ratification of the 1987 Philippine Constitution, to represent LGU interests in policy debates.

- (vi) implementation of capacity development plans for the League of Provinces, League of Municipalities, and League of Cities, focusing primarily on their policy advocacy functions.

12. **Component B:** This will support more effective and transparent LGU budget processes and public expenditure management. Key activities in expenditure management will include (i) improved personal service expenditure policies; and (ii) in select LGUs, application of medium-term expenditure frameworks and output-based budgeting techniques. Support for a more transparent budget review, monitoring, and evaluation process, increasing citizen participation in the budget process, will include (i) support for the roll-out of the e-LGAS; (ii) support for the creation of internal audit functions; (iii) an assessment of progress in implementing new procurement practices, with support for improved implementation as required; and (iv) support for implementing the Local Government Performance Measurement System.

13. **Component C:** This will strengthen LGU financial capacity to mobilize revenues and facilitate the diversification of local borrowings. The TA will support expanded access to credit and bond markets through steps that include:

- (i) undertaking a creditworthiness assessment for each participating LGU;
- (ii) developing and implementing an action plan for strengthening fiscal management with targeted training on borrowing strategies and debt management;
- (iii) examining options of creditworthy LGUs to access the LGU bond market, with additional training in bond issuance; and
- (iv) preparing proposals and financing packages for key investment initiatives, with supportive financing structures that may include official development assistance, commercial borrowing, bond flotation, public-private partnership, and build-operate-transfer arrangements. Possible financing sources include DOF's recent introduction of program lending to LGUs, to support policy reforms in LGUs while providing a new funding source for investment projects.⁹

14. On the taxation side, the TA will support:

- (i) measures to tap additional resources;
- (ii) improvements in the administration of existing taxes, especially the real property tax and business tax;
- (iii) improved management of LGU properties to maximize resources while maintaining a conducive environment for private sector development;
- (iv) training in revenue estimation; and
- (v) developing an LGU revenue manual that can be utilized with other LGUs.

C. Cost and Financing

15. The TA is estimated to cost \$2,575,000 equivalent, of which \$495,000 is foreign exchange cost and \$2,080,000 equivalent is local currency cost. The Government has requested ADB to finance \$1,800,000 equivalent, covering all of the foreign exchange cost and \$1,305,000 equivalent of the local currency cost. The TA will be financed by ADB on a grant basis through ADB's TA funding program. The Government will finance the remaining local-currency cost, equivalent to \$775,000, covering administrative and support costs including

⁹ The first such lending was a four-tranche, P120 million program loan to the province of Negros Occidental to support procurement reforms in eight out of 13 component cities and 12 out of 19 municipalities.

salaries of counterpart staff, secretarial support, supplies, office accommodation, local transportation, miscellaneous costs for training courses, and per diems associated with attendance at such events. Details of the cost estimates are set out in Appendix 2.

D. Implementation Arrangements

16. The Executing Agency for the TA will be DILG. A steering committee will consist of DILG, DOF, Department of Budget and Management (DBM), National Economic and Development Authority, and representatives of the League of Provinces and League of Municipalities. DILG will be the Implementing Agency for component A. DBM will be the Implementing Agency for component B. The Bureau of Local Government Finance of the DOF will be the Implementing Agency for component C. DILG will coordinate with DBM, DOF, National Economic and Development Authority, and the LGUs. The steering committee will meet at least quarterly, at which time written project assessments of progress in implementation, including recommendations of action to be undertaken to correct problems, will be reviewed for discussion with the ADB project officer and project team leader.

17. The TA will be implemented over a period of 24 months commencing in June 2006, with completion expected by May 2008. To implement the TA, the following consulting services will be required: 16 person-months of international consultancy and 184 person-months of domestic consultancy in the areas of local governance and decentralization; intergovernmental fiscal relations; tax administration, budgeting, expenditure, and financial management; public administration and management; organizational restructuring; human resource management; public-private partnerships and structured finance; development financing, policy reform, monitoring and evaluation, and participation; and information and communication technology (ICT). A consulting firm providing all the consulting services will be engaged by quality- and cost-based selection. All recruitment and engagement will undertaken in accordance with ADB's *Guidelines on the Use of Consultants* as may be amended from time to time, and other arrangements satisfactory to ADB for the recruitment of domestic consultants. The outline terms of reference are attached as Appendix 3. ICT equipment will be procured by the consultants, in accordance with procedures acceptable to ADB, to help the selected provinces implement the TA. After completion of the TA, the equipment will be transferred to the provinces in which it was used.

18. Within 1 month of the first TA consultants being fielded, an inception report will be required to outline the framework and processes to implement the TA. Participating LGUs will be selected no later than by the end of month 2. Reports on progress, upcoming plans, and issues to be resolved will be submitted by the team leader to the steering committee and ADB before the end of each project quarter. More detailed reports will be submitted at the end of each project year. Processes and lessons learned under the TA will be documented into knowledge products and tools for sharing and replication.

IV. THE PRESIDENT'S RECOMMENDATION

19. The President recommends that the Board approve the provision of technical assistance not exceeding the equivalent of \$1,800,000 on a grant basis to the Government of the Philippines for Local Governance and Fiscal Management Project.

DESIGN AND MONITORING FRAMEWORK

Design Summary	Performance Targets/Indicators	Data Sources/Reporting Mechanisms	Assumptions and Risks
<p>Impact</p> <p>Fiscal consolidation and poverty reduction are supported through improved service delivery by LGUs and achieved without any increase in the share of domestic revenues transferred to them by the Government.</p> <p>The decentralization process is strengthened through improved implementation of the current system and the preparation of proposals for revision of the legal framework.</p>	<p>The share of domestic revenues transferred to LGUs does not increase.</p> <p>LGU capital expenditures increase in real terms.</p> <p>LGU operating expenditures not related to personnel increase in real terms.</p> <p>Executive Order 444 is smoothly implemented.</p> <p>Proposals for LGC revision are submitted.</p>	<p>DOF budget reports</p> <p>Local government annual reports</p> <p>Commission on Audit report on LGU budget outcomes</p> <p>Consultation with DILG and LGU leagues</p> <p>Staff monitoring</p>	
<p>Outcomes</p> <p>(1) Participating LGUs gain enhanced access to own resources from traditional sources such as taxes, fees, and LGU GOCC income.</p> <p>(2) In participating LGUs, LGU access to nontraditional resources, including bank loans, bonds, and build-operate-transfer arrangements, is enhanced.</p> <p>(3) Improved LGU expenditure and financial management.</p>	<p>At least a 5% increase per year in total real income from taxes, fees, LGU GOCC income, and other non-borrowed sources in all participating LGUs, in aggregate.</p> <p>At least a 5% increase per year in total revenues from nontraditional sources in all participating LGUs, in aggregate.</p> <p>The number of new investment projects financed by credit or bond issuance increases by 5% annually in all participating LGUs, on aggregate.</p> <p>A lower ratio of personnel expenditures to capital outlays supporting public investment programs.</p>	<p>LGU budget reports</p> <p>Commission on Audit report on LGU budget outcomes</p> <p>LGU budget reports</p> <p>Commission on Audit report on LGU budget outcomes</p> <p>LGU budget reports</p> <p>Commission on Audit report on LGU budget</p>	<p>Assumptions</p> <ul style="list-style-type: none"> • The tax base is maintained at current level, or expanded, due to economic growth. • The ability of local leadership to engender cooperation towards reform. • The availability of attractive incentives to reforming LGUs. • Parallel work taking place in the Government improves or at least maintains the regulatory environment for LGU access to nontraditional resources. • LGUs are willing to institute improvements in internal administrative operations.

Design Summary	Performance Targets/Indicators	Data Sources/Reporting Mechanisms	Assumptions and Risks
(4) The legal framework for decentralization is clarified and improved.	<p>An internal audit function is established and/or strengthened in at least 50% of participating LGUs.</p> <p>The Local Government Performance Measurement System is implemented by all participating LGUs.</p> <p>Budget information is released prior to budget approval, and periodic updates are released during the fiscal year.</p> <p>Executive Order 444 is successfully implemented and functions currently assumed by NGAs are transferred to LGUs.</p> <p>Proposals for making intergovernmental fiscal relations among different levels of LGUs are submitted in participating provinces, and some are implemented.</p> <p>An in-depth analysis of further steps for decentralization, including LGC amendments and revisions to the IRA process and formula, is submitted to the Government and LGU leagues.</p>	<p>outcomes</p> <p>Staff monitoring, discussions with DILG and LGU leagues</p> <p>Staff monitoring and reporting</p> <p>Staff monitoring, discussions with DILG and LGU leagues</p> <p>Staff monitoring and reporting, with the usefulness of reports to be assessed through discussions with national Government counterparts and LGU leagues.</p> <p>Staff monitoring and reporting, with usefulness of reports to be assessed through discussions with national Government counterparts and LGU leagues.</p>	<ul style="list-style-type: none"> • Local leaders are able to engender cooperation towards organizational reform. • Attractive incentives to reforming LGUs are available. • The Government issues the necessary implementing executive orders. • NGAs cooperate in devolving functions, personnel, and physical assets as mandated. • LGUs have capacity to mainstream devolved functions in their organizations and operations. • Provincial and component LGU leaders are prepared to implement changes in revenue-sharing arrangements in at least a significant number of participating provinces.
<p>Outputs</p> <p>Overall:</p> <p>Criteria for selection of participating LGUs</p> <p>Selection of participating LGUs</p>	<p>Criteria are developed.</p> <p>Three provinces with component LGUs are selected.</p>		

Design Summary	Performance Targets/Indicators	Data Sources/Reporting Mechanisms	Assumptions and Risks
<p>Component A:</p> <p>Participating LGUs operating under fully devolved NGA functions and resources in accordance with Executive Order 444</p> <p>(1) An in-depth study of the current status of decentralization, with recommendations for revisions of the LGC</p> <p>(2) Based on work in the provinces, develop proposals for the reform of inter-governmental fiscal relations among different levels of LGUs, and assist with implementation</p>	<p>Transfer of functions and resources from NGAs to pilot LGUs completed by end of TA.</p> <p>A local ordinance approving mainstreaming of devolved functions and resources issued by month 15.</p> <p>Devolved functions and resources mainstreamed in the LGU operations and budgets by end of TA.</p> <p>The study is submitted by month 6.</p> <p>Useful proposals are submitted.</p> <p>Implementation is piloted in one or more provinces, and the results are presented for application in other provinces.</p>	<p>Executive order accomplishment and status reports</p> <p>Local ordinance document</p> <p>System audit</p> <p>Staff monitoring and reporting, with the usefulness of the study to be assessed through discussions with national Government counterparts and LGU leagues.</p> <p>Staff review, with the usefulness of proposals to be determined in consultation with LGUs and LGU leagues.</p>	<ul style="list-style-type: none"> • The national Government issues the necessary implementing executive orders. • NGAs cooperate in devolving functions, personnel, and physical assets as mandated. • LGUs have the capacity to mainstream devolved functions in their organizations and operations. • Provincial and component LGU leaders and legislatures are prepared to implement changes in revenue sharing arrangements.
<p>Component B:</p> <p>(1) Development of an improved personnel services expenditure policy for LGUs</p> <p>(2) Training in revenue and expenditure estimation</p> <p>(3) For selected LGUs, training in the use of medium-term expenditure frameworks and output-based budgeting</p>	<p>The policy is developed and implemented in 34% of participating LGUs.</p> <p>Training is delivered</p> <p>LGUs are selected, and training is delivered.</p>	<p>Staff reports, LGU annual reports, LGU budget reports, Commission on Audit LGU budget reports</p> <p>Staff reports</p> <p>Staff reports</p>	<ul style="list-style-type: none"> • LGUs are willing to institute improvements in internal administrative operations. • Local leaders are able to engender cooperation towards organizational reform. • The availability of attractive incentives to reforming LGUs.

Design Summary	Performance Targets/Indicators	Data Sources/Reporting Mechanisms	Assumptions and Risks
<p>(4) Action plan to implement e-LGAS and Local Government Performance Measurement System</p> <p>(5) Action plan for creating an effective internal audit function in LGUs where one is lacking</p> <p>(6) More efficient procurement process and improved quality of procurement outputs</p>	<p>Action plans are developed and the e-LGAS and Local Government Performance Measurement System are implemented in 90% of participating LGUs by end of project.</p> <p>A sustainable internal audit function is established in 50% of LGUs in which one is lacking.</p> <p>Local ordinance installing procurement reforms issued by month 12.</p>	<p>Staff reports, LGU annual reports, consultations with the Commission on Audit and DILG</p> <p>Local ordinances Staff reports Consultations with the Commission on Audit</p> <p>Local ordinances, staff reports, consultations with DBM</p> <p>System audit</p>	
Component C:			
<p>(1) Revenue mobilization action plans for participating LGUs</p>	<p>Action plans are submitted and implemented.</p>		<ul style="list-style-type: none"> • LGUs are willing to institute improvements in internal administrative operations.
<p>(2) New LGU tax manual</p>	<p>Tax manual is produced.</p>		<ul style="list-style-type: none"> • Local leaders are able to engender cooperation towards organizational reform.
<p>(3) Design and implementation of a resource mobilization training program</p>	<p>Training is implemented in coordination with the Local Government Academy and other institutions.</p>	<p>Staff reports</p>	<ul style="list-style-type: none"> • Attractive incentives to reforming LGUs are available.
<p>(4) Action plans on more effective use of revenues from LGU GOCCs</p>	<p>Action plans are submitted and implemented.</p>	<p>Staff reports, LGU annual reports</p>	
<p>(5) Action plans for improved LGU tax administration</p>	<p>Action plans are submitted and implemented.</p>	<p>Staff reports, LGU annual reports</p>	
<p>(6) Creditworthiness assessments of all participating LGUs</p>	<p>Creditworthiness assessments are conducted.</p>	<p>Staff reports</p>	
<p>(7) Creditworthiness action plans for all participating LGUs</p>	<p>Creditworthiness action plans are implemented and regularly monitored.</p>	<p>Staff reports, LGU annual reports, consultation with commercial banks</p>	
<p>(8) Debt management manual for LGUs</p>	<p>The manual is produced.</p>	<p>Staff reports</p>	

Design Summary	Performance Targets/Indicators	Data Sources/Reporting Mechanisms	Assumptions and Risks
(9) Assistance with development of investment proposals and financing packages for LGUs	Proposals are produced and financing packages arranged for 10 LGUs per year.	Staff reports, LGU annual reports	
Activities With Milestones Overall 1.1 Develop selection criteria and select 3 participating provinces (months 1–2) Components A and B 1.1 Field consultants in all three participating subregions and/or provinces (month 3) 1.2 Assess tax policy, tax administration, creditworthiness, and budget processes and financial management in the subregions and provinces (months 4–5) 1.3 Develop comprehensive action plans (month 6) 1.4 Launch action plan implementation (month 7) 1.5 Conduct public consultation, plan launch, advocacy, and public orientation in each area (months 8–18) 1.6 Provide advisory assistance in the local legislation process (months 12–15) 1.7 Provide advisory assistance and hand-holding services to LGU technical units in the management of plan implementation (months 8–24) Component C 1.8 Formulate framework and devolution approach (months 4–5) 1.9 Identify functions, programs, and activities of national government agencies to be devolved (months 5–6) 1.10 Develop devolution implementation plan (months 6–7) 1.11 Implement transfer of functions and resources to LGUs (months 8–22) 1.12 Post devolution performance evaluation (months 23–24) 1.13 Submit in-depth study of state of decentralization (month 6) 1.14 Conduct workshops to present findings of study (months 7–8) 1.15 Revise study and formulate concrete legislative measures to implement findings (months 8–9) 1.16 Prepare capacity development plans for the League of Provinces, League of Municipalities, and League of Cities, focusing on their policy advocacy functions. (month 4) 1.17 Implement league capacity development plans (months 6–12)			Inputs <ul style="list-style-type: none"> • ADB--consulting services (16 person-months of international and 184 person-months of domestic)\$1,470,000, workshops and seminars \$150,000, equipment \$25,000, • Government-- administrative and support costs including contingencies \$775,000, counterpart contributions including staff time, office space, workshop support, and others

DBM = Department of Budget and Management, e-LGAS = electronic local government accounting system, GOCC = government owned and controlled corporation, IRA = internal revenue allotment, LGC = Local Government Code of 1991, LGU = local government unit, NGA = national government agency, TA = technical assistance.

COST ESTIMATES AND FINANCING PLAN
(\$'000)

Item	Foreign Exchange	Local Currency	Total Cost
A. Asian Development Bank Financing^a			
1. Consultants			
a. Remuneration and Per Diem			
i. International Consultants	400.0	0.0	400.0
ii. Domestic Consultants	0.0	1,000.0	1,000.0
b. International and Local Travel	45.0	25.0	70.0
c. Reports and Communications	0.0	20.0	20.0
2. Equipment	0.0	25.0	25.0
3. Training, Seminars, and Conferences			
a. Training Program/Workshops	0.0	150.0	150.0
4. Miscellaneous Administration and Support Costs	0.0	20.0	20.0
5. Contingencies	50.0	65.0	115.0
Subtotal (A)	495.0	1,305.0	1,800.0
B. Government Financing			
1. Office Accommodation and Transport	0.0	175.0	175.0
2. Remuneration and Per Diem of Counterpart Staff	0.0	530.0	530.0
3. Others	0.0	70.0	70.0
Subtotal (B)	0.0	775.0	775.0
Total	495.0	2,080.0	2,575.0

^a Financed by the Asian Development Bank's technical assistance funding program.
Source: Asian Development Bank estimates.

OUTLINE TERMS OF REFERENCE FOR CONSULTING SERVICES

A. Introduction

1. Consultant services will be engaged under all three components of this technical assistance (TA). A team leader, expected to be a national consultant, will oversee implementation of all components and lead the work on one of the components. It is expected that some consultants will work on more than one component. International consultants will be brought in as needed for work on all components and to provide expertise in the most current international practices in relevant aspects of decentralization and local government financial management. Teams of local consultants will work on all three sets of issues in participating provinces, (i) analyzing local conditions, (ii) identifying key areas for improvement and preparing action plans to achieve those improvements, and (iii) assisting with the implementation and monitoring of action plans. They will also organize workshops to facilitate exchanges of experience among the participating local government units (LGUs) and between them and representatives of other regions.

B. Engagement of Consultants

2. Consultants will be recruited in accordance with the *Guidelines on the Use of Consultants* of the Asian Development Bank (ADB) or other procedures acceptable to ADB for the selection of international and domestic consultants.

C. Staffing

3. Consulting services will be provided over a period of 24 months and total approximately 200 person-months, including approximately 16 person-months of international consultancy and 184 person-months of domestic consultancy.

4. **Team Leader.** The team leader, a national consultant to be employed for the period of the project, should be an experienced expert in Philippine LGU finance and administration with strong analytical skills and experience in managing projects. Communication skills and the ability to deal effectively with government offices, both national and local, are essential. This person will do the following:

- (i) Provide overall intellectual leadership, oversight, and direction to the project team.
- (ii) Assist in finalizing selection criteria for participating LGUs and in the selection process itself.
- (iii) Report as required to the Department of Interior and Local Government (DILG), the Executing Agency, and to the steering committee and ADB project officer.
- (iv) Coordinate timing and selection when recruiting short-term experts in consultation with the Government and ADB project officer.
- (v) Oversee and ensure the effectiveness of project training activities.
- (vi) Lead the technical work in component A or C.
- (vii) Act as the point of contact between DILG, Implementing Agencies, and ADB in regard to project activities.

1. Component A

5. Approximately 4 person-months of international consultancy and 38 person-months of domestic consultancy will be needed in areas of expertise expected to include the following:
- (i) decentralization policy experts with broad international experience in designing and implementing effective fiscal decentralization programs;
 - (ii) intergovernmental fiscal relations experts with prior experience working on fiscal transfers and revenue sharing between the national Government and local governments, and between different levels of local governments, including knowledge of current international practice in this field;
 - (iii) change-management experts with a track record of successful support for implementing government restructuring and able to assist the Government with planning the implementation of Executive Order 444;
 - (iv) LGU tax policy experts who know how to design effective tax measures in local governments, factoring in implications of revenue sharing arrangements; and
 - (v) an institutional development expert with successful experience in developing advocacy functions in nongovernment and other organizations.
6. Tasks to be undertaken under this component will include the following:
- (i) Undertake an in-depth review of the first 15 years of decentralization, identifying successes, failures, and areas in which action needs to be taken to advance the decentralization process further. In light of the Government's consideration of a possible shift to a federal system, the findings and recommendations of this review should be relevant under both the current system and a possible federal system.
 - (ii) Aid in preparing the devolution framework in accordance with Executive Order 444, including developing the methodology for assessing the various sectors, defining the proper vertical compartmentalization of functions between the Government and LGUs, and identifying the functions that will no longer be exercised by the national government agencies.
 - (iii) Prepare a change-management plan and timetable to help national government agencies deal with the process of transferring functions, staff, operations, and resources to LGUs.
 - (iv) Assess current practices by which participating provinces share revenues with their municipalities and develop proposals for their improvement.
 - (v) Support the development and implementation of revisions in intraprovincial revenue sharing as permitted by law.
 - (vi) Assess the impact of the current internal revenue allotment formula and procedures on revenue adequacy, predictability, and collection incentives in participating LGUs and develop proposals for reforming internal revenue allotment.
 - (vii) Prepare and help implement capacity development plans for LGU leagues, focusing on their policy advocacy functions.

2. Component B

7. Approximately 6 person-months of international consultancy and 74 person-months of domestic consultancy will be needed to strengthen budgeting and expenditure management in participating LGUs. It is expected that the expertise needed will include the following:
- (i) LGU financial management experts with experience in LGU internal audit functions;

- (ii) LGU budget specialists with practical experience in strengthening LGU budgeting policies covering personal service expenditures, capital expenditure planning, and other budget items;
- (iii) medium-term expenditure management experts who have implemented such approaches in LGUs in Philippines and/or elsewhere;
- (iv) LGU accounting specialists with expertise in Philippine LGU accounting systems and familiarity with the new electronic local government accounting system (e-LGAS) developed by the Commission on Audit; and
- (v) a monitoring and evaluation specialist familiar with LGU performance assessment methodologies and the Local Government Performance Measurement System of the DILG.

8. Specific tasks may include the following, though a detailed work plan for each participating province will be prepared based on its specific requirements:

- (i) Develop improved policies on personal service expenditures.
- (ii) If appropriate, conduct training on the application of medium-term expenditure frameworks and program budgeting techniques.
- (iii) Support a transparent budget review, monitoring, and evaluation process that increases citizens' participation in the budget process, including the publication in local media of budget plans prior to their approval and of periodic reports on budget implementation.
- (iv) Support the effective use of the e-LGAS.
- (v) Support the creation of an effective internal audit function.
- (vi) Support implementation of the new Local Government Performance Measurement System being rolled out by DILG.

3. Component C

9. Approximately 6 person-months of international consultancy and 72 person-months of domestic consultancy will be needed to strengthen resource mobilization in participating LGUs. It is expected that the needed expertise will include the following:

- (i) LGU finance experts, with experience in LGU financial planning, debt management, and borrowing strategy, who will lead the development of creditworthiness assessments and implementation of new LGU fiscal frameworks to enhance creditworthiness;
- (ii) LGU infrastructure specialists with experience in planning LGU infrastructure projects;
- (iii) LGU tax administration experts with experience in improving the collection of the real property tax and business tax, especially in the Philippines, as well as broader knowledge of effective tax administration in local governments;
- (iv) LGU tax policy experts with practical knowledge of designing effective tax measures in local governments of diverse financial circumstances;
- (v) intergovernmental fiscal relations experts with prior experience working on fiscal transfers and revenue sharing between the national Government and local governments, and between different levels of local governments, including knowledge of current international practice in this field;
- (vi) project finance experts with experience in developing project finance proposals, including analyzing the financial requirements of an investment, preparing proposals, and presenting proposals to potential financing sources; and
- (vii) LGU bond market experts with experience in working with LGU governments who access bond markets in the Philippines and elsewhere.

10. Specific tasks may include the following, though a detailed work plan for each participating province will be prepared based on its specific requirements:

- (i) Prepare and implement measures to tap additional resources, based on initial work with the LGU to identify revenue sources that are not being fully utilized.
- (ii) Develop and implement measures to improve tax administration and collection.
- (iii) Provide assistance for efficiently managing municipal properties to maximize resources while maintaining a conducive environment for private sector development.
- (iv) Provide training in revenue estimation.
- (v) Develop an LGU revenue manual that can be used by other LGUs.
- (vi) Undertake an LGU creditworthiness assessment based on criteria used by banks and the Bureau of Local Government Finance, and for level 1 LGUs by the Local Government Unit Guarantee Corporation.
- (vii) Develop an action plan to achieve creditworthiness for implementation during the course of TA, including targeted training on borrowing strategies and debt management (a progress to be monitored every 6 months).
- (viii) For selected LGUs, scale up the action plan to target their ability to access the LGU bond market, with the same monitoring and additional training on bond issuance.
- (ix) Identify key investment initiatives contained in capital budgets and development plans for financing and implementation, in close coordination with participating LGUs and the NG, and so expand the program lending to LGUs recently introduced by the Department of Finance's Municipal Development Fund Office, thereby supporting policy reforms in LGUs while providing a new funding source for investment projects.