



Report and Recommendation of the President to the Board of Directors

Project Number: 52173-003
August 2021

Proposed Policy-Based Loan for Subprogram 2 Republic of the Philippines: Local Governance Reform Program

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Asian Development Bank

CURRENCY EQUIVALENTS

(as of 30 July 2021)

Currency unit	–	peso/s (₱)
₱1.00	=	\$0.0199072323
\$1.00	=	₱50.233000

ABBREVIATIONS

ADB	–	Asian Development Bank
BLGF	–	Bureau of Local Government Finance
COVID-19	–	coronavirus disease
DILG	–	Department of the Interior and Local Government
DOF	–	Department of Finance
GAD	–	gender and development
GAD-PBMS	–	gender and development plan budget monitoring system
GDP	–	gross domestic product
IRA	–	internal revenue allotments
LGC	–	Local Government Code
LGU	–	local government unit
LIFT	–	LGU integrated financial tool
PDMF	–	project development and monitoring facility
PDP	–	Philippine Development Plan
PFM	–	public financial management
PPP	–	public–private partnership
SDG	–	Sustainable Development Goal
SGLG	–	Seal of Good Local Governance

NOTES

- (i) The fiscal year (FY) of the Government of the Philippines ends on 31 December. “FY” before a calendar year denotes the year in which the fiscal year ends, e.g., FY2021 ends on 31 December 2021.
- (ii) In this report, “\$” refers to United States dollars.

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PROGRAM AT A GLANCE

1. Basic Data		Project Number: 52173-003	
Project Name	Local Governance Reform Program (Subprogram 2)	Department/Division	SERD/SEPF
Country	Philippines	Executing Agency	Department of Finance
Borrower	Republic of the Philippines		
Country Economic Indicators	https://www.adb.org/Documents/LinkedDocs/?id=52173-003-CEI		
Portfolio at a Glance	https://www.adb.org/Documents/LinkedDocs/?id=52173-003-PortAtaGlance		
2. Sector	Subsector(s)	ADB Financing (\$ million)	
✓ Public sector management	Decentralization		400.00
		Total	400.00
3. Operational Priorities		Climate Change Information	
✓ Addressing remaining poverty and reducing inequalities		GHG reductions (tons per annum)	0.000
✓ Accelerating progress in gender equality		Climate Change impact on the Project	Low
✓ Tackling climate change, building climate and disaster resilience, and enhancing environmental sustainability			
✓ Strengthening governance and institutional capacity		ADB Financing	
		Adaptation (\$ million)	54.74
		Mitigation (\$ million)	31.59
		Cofinancing	
		Adaptation (\$ million)	0.00
		Mitigation (\$ million)	0.00
Sustainable Development Goals		Gender Equity and Mainstreaming	
SDG 1.5, 1.a, 1.b		Effective gender mainstreaming (EGM)	✓
SDG 5.b, 5.c			
SDG 13.a		Poverty Targeting	
SDG 16.6, 16.7		General Intervention on Poverty	✓
SDG 17.9			
4. Risk Categorization:	Complex		
5. Safeguard Categorization	Environment: C	Involuntary Resettlement: C	Indigenous Peoples: C
6. Financing			
Modality and Sources		Amount (\$ million)	
ADB		400.00	
Sovereign Programmatic Approach Policy-Based Lending (Regular Loan): Ordinary capital resources		400.00	
Cofinancing		0.00	
None		0.00	
Counterpart		0.00	
None		0.00	
Total		400.00	
Currency of ADB Financing: US Dollar			

I. THE PROPOSAL

1. I submit for your approval the following report and recommendation on a proposed policy-based loan to the Republic of the Philippines for subprogram 2 of the Local Governance Reform Program.¹

2. The program aims to strengthen the capacities of local government units (LGUs) to deliver high-quality public services. It builds upon the government's local governance reform priorities to (i) strengthen the local governance framework, (ii) modernize and professionalize subnational public financial management (PFM), and (iii) improve the LGU financing and investment framework.

II. PROGRAM AND RATIONALE

A. Background and Development Constraints

3. **Programmatic approach and budget support.** The program embraces a programmatic approach to align the Asian Development Bank's (ADB) support with the government's medium- to long-term efforts to foster more accountable, more transparent, and better public service delivery by LGUs. In turn, services will boost local economic development and help reduce poverty and regional disparities. ADB approved the programmatic approach, comprising two subprograms, on 13 November 2019.² Subprogram 1 was supported through a loan of \$300 million, and consisted of 15 prior actions that empowered and equipped LGUs to meet the needs of citizens, improved the capacity of LGUs to raise their own revenue, and lowered the cost of doing business for the private sector (footnote 2). All the prior actions completed in subprogram 1 have been maintained, with no reversals. Subprogram 2 builds upon the achievements under subprogram 1 and the tools and measures under ADB's related project loan.³ The post-program partnership framework, 2021–2024 will enable ADB to continue supporting the government's local governance reform agenda.

4. **Local governance reform to support coronavirus disease pandemic recovery.** Before the coronavirus disease (COVID-19) pandemic, the Philippines sustained strong growth averaging 6.4% in 2010–2019. Macroeconomic policy was appropriate to support economic growth in the medium term.⁴ The country's debt profile was assessed to be sustainable, with sound fiscal risk and public debt management strategies in place.⁵ The Philippines consistently reduced the national poverty rate from 26.6% in 2006 to 16.6% in 2018;⁶ however, income inequality and regional disparities were still prevalent as the Gini coefficient stood at 0.43 in 2018, exceeding that of regional peers and relatively unchanged from 0.44 in 2015. For example, the poverty rate remained considerably higher in remote regions such as the Bangsamoro Autonomous Region in Muslim Mindanao (61.3%), Zamboanga Peninsula (32.7%), and Eastern Visayas (30.9%). Now, the COVID-19 pandemic stands to erode the gains made in poverty reduction and exacerbate regional and gender-based disparities. Gross domestic product (GDP)

¹ Subprogram 2 is the final subprogram.

² ADB. 2019. [Report and Recommendation of the President to the Board of Directors: Proposed Programmatic Approach and Policy-Based Loan for Subprogram 1 to the Republic of Philippines for the Local Governance Reform Program](#). Manila.

³ ADB. 2020. [Report and Recommendation of the President to the Board of Directors: Proposed Loan to the Republic of Philippines for the Local Governance Reform Project](#). Manila.

⁴ International Monetary Fund Assessment Letter (accessible from the list of linked documents in Appendix 2).

⁵ International Monetary Fund. 2020. [Philippines: 2019 Article IV Consultation—Press Release and Staff Report](#). Washington, DC.

⁶ Philippine Statistics Authority. 2020. [2018 Family Income and Expenditure Survey](#). Manila.

contracted by 9.6% in 2020 against the original forecast of 6.2% growth.⁷ ADB estimates that the national poverty rate could increase to about 20% in 2020 from 16.6% in 2018, which equates to an additional 5.5 million people falling into poverty. Women and girls are particularly vulnerable as they face challenges to their well-being, such as reduced access to healthcare services, gender-based violence, and economic insecurity.⁸ Recognizing the role of LGUs in pro-poor and pro-women responses to COVID-19, the government has stepped up local governance reform as part of the national strategies for social and economic recovery.⁹ Hence, strong LGU capacity to manage fiscal resources and deliver public services backed by a robust policy framework is critical to reinstating strong growth trajectories.

Box 1: Mandanas Ruling and Executive Order Number 138

The Supreme Court ruling on the Mandanas–Garcia case (Mandanas ruling), finalized on 10 April 2019, mandates that the base national government revenues against which the mandated 40% internal revenue allotments to local government units (LGUs) are determined is not limited to national internal revenue taxes collected by the Bureau of Internal Revenue but includes all national taxes including tariffs, customs duties, and other taxes, fees, and charged collected by agents of the national government including the Bureau of Customs. This will facilitate LGUs to take on more responsibilities in line with the 1991 Local Government Code, which would also be aligned with the decentralization principle of funding following functions. The government envisages implementation of the Mandanas ruling as a key instrument of the coronavirus disease pandemic response, as it contains measures that would help improve the quality of local public service delivery and reduce poverty and unemployment in local communities through local governance reforms.

In response to the need to accelerate local governance reforms and organizational transitions of the national government and LGUs, the President of the Philippines, on 1 June 2021, signed the Executive Order Number 138 titled Full Devolution of Certain Functions of the Executive Branch to Local Governments, Creation of A Committee on Devolution, and For Other Purposes. The Executive Order directs the full devolution of functions from the national government to LGUs in line with the Mandanas ruling. It will ensure that the policy of decentralization as enshrined in the Constitution and the 1991 Local Government Code, as well as the increase in the internal revenue allotments for LGUs as provided for in the Mandanas ruling, will be carried out systematically and smoothly, by: (i) establishing oversight and monitoring mechanisms to resolve issues and concerns that may arise in the implementation of the Mandanas ruling; (ii) setting up the Growth Equity Fund to address issues on marginalization, unequal development, high poverty incidence, and disparities in capacities of LGUs; and (iii) adopting transition plans to ensure the continuous service delivery by the national government agencies and LGUs.

LGUs = local government units.
Source: Asian Development Bank.

5. Need for gearing up local governance reforms. Subprogram 2 comes at a critical juncture for the Philippines, when public attention to, and demand for, devolution of public services is increasing. The 1991 Local Government Code (LGC) underpinned decentralization of service delivery, taxing powers, and certain regulatory functions. Local fiscal performance since then has been strengthened gradually, yet consistently. LGUs' locally sourced revenue grew by 22.6% during 2017–2019. However, LGUs still rely heavily on internal revenue allotments (IRA) from the national government as their main source of income, thereby limiting fiscal responsibility and autonomy. Own-source revenue accounted for 32% of total LGU revenue in 2019—below the

⁷ Philippine Statistics Authority. 2021. [Press Release: Q4 2020 National Accounts of the Philippines](#). Manila.

⁸ United Nations Women. 2020. [Gender Snapshot: COVID-19 in the Philippines](#). Bangkok.

⁹ Inter-Agency Task Force. 2020. [We Recover as One](#). Manila. Under Republic Act 11494, known as Bayanihan to Recover as One Act, the government has allocated ₱1.5 billion (\$31 million) for the Local Government Support Fund to support LGUs in their COVID-19 relief efforts.

government target of 37% of total local revenue by 2022—and was particularly low among provinces (16%) and municipalities (18%). Moreover, the absorptive capacities of LGUs need to be further strengthened to support the transition to full devolution of public services as necessitated by the Mandanas ruling.¹⁰ The Department of Budget and Management estimates that the ruling will increase the IRA in fiscal year (FY) 2022 by 38% in comparison with FY2021, equivalent to \$5.5 billion (₱263 billion) or 1% of GDP.¹¹ As a result, the need to strengthen local governance reform has accelerated to ensure that additional fiscal resources for LGUs lead to improved service delivery.

6. **Binding constraints.** The government has identified the challenges to be tackled to realize the goal of people-centered, clean, and efficient local governance. These challenges, which still hinder the ability of the LGUs to fulfill the 1991 LGC mandates and to deliver quality local services, include: (i) weaknesses in implementing and monitoring frameworks for LGUs; (ii) ineffective tools and incentives for LGUs to deliver high-quality public services; and (iii) insufficient participation of the private sector, citizens, and stakeholders in local service delivery.¹²

7. **Weaknesses in implementing and monitoring frameworks for local government units.** The 1991 LGC and its subsequent amendments have provided regulatory frameworks for LGUs to become self-reliant, and transparent and accountable to their citizens. However, central–local and interlocal coordination remains inadequate because of unclear and overlapping roles and functions, hampering the ability of LGUs to perform their mandates (e.g., raising local revenues, delivering public services, and preparing for emerging challenges such as gender development and climate change). Likewise, gender-responsive planning and budgeting need to be improved, and local planning needs to be more aligned with national and international development goals. Effective monitoring is needed to track performance against result-oriented performance indicators. The government has taken steps to streamline the roles and functions of national and local governments. However, much work still needs to be done. For instance, while property prices grew by 15% yearly in 2009–2018, real property taxes collected by LGUs declined by more than 8% annually during the same period.¹³ Many LGUs have not been able to fulfill the statutory expenditure requirement, which obliges them to devote at least 20% of their annual budgets to development projects and at least 5% to gender and development (GAD).¹⁴

8. **Ineffective tools and incentives for local government units.** As of 2018, the budget execution rate among LGUs was low, at 72.2% of the total budget and merely 43.9% for capital outlays, indicating ineffective local service delivery.¹⁵ The low absorptive capacity of LGUs has several causes, such as unclear and overlapping responsibilities of national and local governments; inefficient budget planning and execution; and low capacity to develop programs, projects, and activities. However, under the Mandanas ruling, additional financing will be provided, and more responsibilities and functions will be cascaded from the national government to LGUs. The government has implemented a wide array of measures and tools to improve the absorptive capacities of LGUs. For example, the Standardized Examination and Assessment for Local

¹⁰ Government of the Philippines. 2020. *What Is Mandanas Ruling?* Manila.

¹¹ The estimated impacts of the Mandanas ruling on IRA are preliminary and subject to revisions.

¹² Sector Assessment: Public Sector Management (accessible from the list of linked documents in Appendix 2).

¹³ N. Ramos. 2019. *Assessment of Economic and Financial Impacts of Package 3 Reforms under the Proposed Valuation Reform Act*. Manila: ADB (prepared under ADB. 2016. *Technical Assistance to the Republic of the Philippines for Strengthening Tax and Fiscal Policy Capacity for Inclusive Growth*). Manila.

¹⁴ Joint Memorandum Circular 2017–1 requires at least 20% of annual budgets for social development projects and basic infrastructure. Republic Act 9710 (Magna Carta of Women) requires at least 5% for gender development.

¹⁵ Commission on Audit. 2019. *2018 Annual Financial Report: Local Government Volume I*. Manila.

Treasury Service Program put in place a competency and assessment framework to professionalize local treasurers. The LGU integrated financial tool (LIFT) and a fiscal sustainability scorecard for LGUs were introduced to incentivize local treasurers and budget officers to embrace international best practices for local PFM and to modernize and improve local fiscal reporting. However, these tools and incentives emphasize compliance with legal mandates rather than improving the quality of public services. Therefore, LGU capacities need to be further strengthened to meet service standards such as citizen satisfaction and accountable gender and social development.

9. Insufficient participation of the private sector, citizens, and stakeholders in local service delivery. Filling the fiscal gaps and meeting the expenditure needs of LGUs remain a challenge on many fronts. LGUs rely heavily on IRA transfers as their main source of financing. The private sector faces high costs of doing business as many LGUs still have not complied with the requirements of the Ease of Doing Business Act. The capacity of LGUs to access private sector financing is typically limited, contributing to poor service delivery. The implementation of the Mandanas ruling in 2022 will increase the opportunity to finance priority development projects and capital expenditures and to improve municipal financing and borrowing. Typically, LGUs pursue public–private partnership (PPP) projects through joint ventures. However, the PPP Center’s project development and monitoring facility (PDMF) can only support local PPP projects under the Build–Operate–Transfer Law which does not cover joint ventures. Many local projects are small and may not have enough economies of scale to attract private sector interest. An innovative approach to private sector participation in these small, yet critical, local projects is needed. Further, LGUs also play a critical role in community relief and recovery from natural hazard events. Disaster risk financing for LGUs needs to be strengthened with effective measurement and monitoring of resilience readiness. Finally, continued efforts are required to amplify citizen feedback, alongside LGU transparency and accountability to citizens.

10. Alignment with government’s national plan and ADB’s priorities. The program is a key part of ADB’s support to help the government ensure people-centered, clean, and efficient local governance, in line with the Updated Philippine Development Plan (PDP), 2017–2022.¹⁶ The program will support the second pillar of ADB’s country partnership strategy, 2018–2023, on promoting local economic development.¹⁷ Subprogram 2 is aligned with the following operational priorities of ADB’s Strategy 2030: (i) reducing remaining poverty and inequalities; (ii) accelerating progress in gender equality and women’s empowerment; (iii) tackling climate change, building climate and disaster resilience, and increasing environmental sustainability; and (iv) strengthening governance and institutional capacity.¹⁸

B. Policy Reform, ADB’s Value Addition, and Sustainability

11. Government’s reform agenda. Since the enactment of the 1991 LGC, the government has made gradual, yet consistent progress in improving the efficiency and transparency of LGUs. In response to the COVID-19 pandemic, the government has begun to accelerate local governance reforms toward devolution of public services and improved delineation of national government and LGU functions. With the 2009 Climate Change Act and the Intended Nationally Determined Contributions under the Paris Agreement, the government envisages the Local Governance Reform Program as a continuing effort to strengthen the country’s resilience to

¹⁶ National Economic and Development Authority. 2021. [Updated Philippine Development Plan, 2017–2022](#). Manila.

¹⁷ ADB. 2018. [Country Partnership Strategy: Philippines, 2018–2023—High and Inclusive Growth](#). Manila. Subprogram 2 is included in the country operations business plan, 2021–2023 of ADB for the Philippines. ADB. 2020. [Country Operations Business Plan: Philippines, 2021–2023](#). Manila.

¹⁸ Contribution to Strategy 2030 Operational Priorities (accessible from the list of linked documents in Appendix 2).

climate change.¹⁹ The PDP, 2017–2022 recognizes improved local governance and fiscal decentralization as the impetus for achieving the Sustainable Development Goals (SDGs). Subprogram 2 will contribute to the following SDGs: (i) end poverty in all its forms everywhere (SDG 1); (ii) achieve gender equality and empower all women and girls (SDG 5); (iii) take urgent action to combat climate change and its impacts (SDG 13); (iv) promote peaceful and inclusive societies for sustainable development; provide access to justice for all; and build effective, accountable, and inclusive institutions at all levels (SDG 16); and (v) strengthen the Global Partnership for Sustainable Development (SDG 17).

12. **Reform accomplishments.** At the inception of the program in 2018, the government agreed to accomplish 19 prior actions as the basis for subprogram 2. There has been no deviation from the indicative policy actions originally established for subprogram 2. During the processing of subprogram 2, 10 prior actions (1, 2, 3, 4, 6, 12, 14–16, and 18) were strengthened to boost gender responsiveness, reflect the progress of implementation beyond expectations, and better capture development impact. All prior actions in subprogram 2 have been accomplished.²⁰

Box 2: Key Accomplishments under the Local Governance Reform Program, Subprogram 2

The government has accomplished the following as part of subprogram 2:

- (i) **Increased fund allocation to support devolution of functions.** Implemented the Mandanas ruling^a to provide LGUs with greater internal revenue allocations and clearer roles and functions from the 2022 national budget, and approved Executive Order Number 138 on Full Devolution of Functions to LGUs to institute a legal framework for the Mandanas ruling;
- (ii) **Expedited measures to boost LGUs' own-source revenue.** Established the property valuation office and the Bureau of Local Government Finance Management Committee to accelerate the implementation and oversight of the real property valuation and assessment reform;
- (iii) **Improved local monitoring.** Rolled out a real-time local development investment program monitoring framework and GAD budget monitoring framework;
- (iv) **Aligned LGU investments to achieve SDGs.** Set aside at least 35% of local funds for GAD, youth development, and local development projects, and aligned them with the national development and investment plans and SDGs;
- (v) **Professionalized local public financial management.** Expanded tools and incentives for LGUs to fill service delivery gaps for women and vulnerable groups; continued to professionalize local treasurers and local budget officers using information technology; and
- (vi) **Strengthened the local investment climate.** Expanded PPP frameworks to promote local PPP project development; reduced the cost of doing business by requiring LGU business processes to comply with the Ease of Doing Business Act, and improved citizen feedback.

GAD = gender and development, LGU = local government unit, PPP = public–private partnership, SDGs = Sustainable Development Goals.

^a The details of the Mandanas ruling and the Executive Order Number 138 on Full Devolution of Functions to LGUs are provided in Box 1.

Source: Asian Development Bank.

13. **Reform area 1: Strengthening the local governance framework for service delivery.** This reform area reinforces existing legal and implementing frameworks to improve central–local and interlocal coordination, and to boost the capacity of LGUs for managing larger intergovernmental fiscal transfers and devolution of public services. The reform area builds upon the accomplishments of subprogram 1 by strengthening LGUs' accountability and responsiveness to the need for service delivery and own-source revenue mobilization. There were five

¹⁹ Climate Change Assessment (accessible from the list of linked documents in Appendix 2).

²⁰ Comparison of Original and Revised Subprogram 2 (accessible from the list of linked documents in Appendix 2).

accomplishments under subprogram 2. First, the government incorporated the increased IRA for LGUs in the preparation of the 2022 national budget in line with the Mandanas ruling, and more clearly delineated national and local government roles.²¹ The government approved Executive Order Number 138 on the Full Devolution of Functions to LGUs to institute a legal framework to implement the Mandanas ruling and transition plans.²² This reform measure prepared LGUs to meet their increased responsibilities for service delivery arising from the increase in IRA shares from FY2022 onward. Second, the government set up the property valuation office and established the Bureau of Local Government Finance (BLGF) Management Committee to oversee the overall implementation of the Real Property Valuation and Assessment Reform and to provide technical and policy advice and coordination support to the Department of Finance (DOF) and agencies concerned with ensuring the reform's success.²³

14. Third, to improve monitoring and coordination, the government rolled out an online system for real-time submission and tracking of the Local Development Investment Program (e-LDIP) and adopted the GAD plan budget monitoring system (GAD-PBMS).²⁴ The e-LDIP and GAD-PBMS enable the national government to track and report local government planning and budgeting, and to mainstream gender perspectives in local government plans. Fourth, the government strengthened local planning and budget frameworks under National Budget Memorandum Number 136, which requires the investment programs of LGUs to align with the PDP, 2017–2022; the Public Investment Program, 2017–2022; and the SDGs. The frameworks mandated that LGUs utilize local budgets to meet statutory expenditure requirements such as at least 5% for GAD, 10% for youth development and empowerment (Sangguniang Kabataan), and 20% for development projects. Last, the national government's oversight of local planning and budgeting was reinforced by formulating provincial results matrixes for the PDP, 2017–2022. The government improved several existing guidelines and manuals²⁵ and provided training to LGUs and regional government offices to strengthen their capacity to review local plans, revenue mobilization, and budgets.

15. **Reform area 2: Modernizing and professionalizing local public financial management.** This reform area addresses bureaucratic weaknesses and inefficiencies in local PFM. Subprogram 1 introduced a wide range of PFM tools and measures to improve local PFM functions, including the Standardized Examination and Assessment for Local Treasury Service Program, the LIFT PFM system, and the Fiscal Sustainability Scorecard. Subprogram 2 continued to professionalize core public finance functions and expand tools and incentives to promote efficient and high-quality delivery of public services. First, the government improved and linked the LGU e-Budget Preparation Module with the BLGF and Department of the Interior and Local Government (DILG) systems, and integrated monitoring of GAD and environmental data. The enhancements enabled LGUs and the national government to produce a consolidated set of PFM data and reports, thereby improving efficiency, transparency, and oversight of local budget

²¹ Under the delineation plan, national government roles will be limited to: (i) setting national policy and service standards; (ii) assisting, overseeing, and monitoring LGUs; and (iii) strengthening capacities of LGUs.

²² Executive Order Number 138 approved on 1 June 2021 is titled Full Devolution of Certain Functions of the Executive Branch to Local Governments, Creation of A Committee on Devolution, and For Other Purposes. The Department of Budget and Management has likewise issued the Local Budget Memorandum Number 82 dated 14 June 2021 to inform LGUs of their indicative national tax allotment shares in FY 2022 and to guide LGUs' preparation of the FY 2022 annual budgets.

²³ DOF's Department Order Number 2 (2021) titled Implementation and Operationalization of Executive Order Number 833 (2019).

²⁴ The Local Development Investment Program allocates LGUs' general budgets to programs, projects, and activities.

²⁵ These include: (i) the updated policy for the Model Local Revenue Code, (ii) the updated Local Treasury Operations Manual, and (iii) the updated guidelines on the assessment of the comprehensive development plans of cities and municipalities.

planning and utilization. Second, the government strengthened the minimum PFM performance standards for the Seal of Good Local Governance (SGLG), which requires LGUs to prioritize gender development and social protection, and bridge service delivery gaps for women and vulnerable groups such as children, the elderly, and people with disabilities. The upgraded SGLG criteria include the fiscal sustainability of LGUs and increased spending on priority sectors such as social protection, health, and education. As of December 2019, 442 LGUs (26% of total LGUs) had passed the new SGLG criteria.

16. The government also introduced five critical capacity development initiatives to further professionalize local treasurers and budget officers: (i) electronic capacity development platforms for building the core competencies of local treasurers and budget officers; (ii) a competency assessment and measurement system for local budget officers;²⁶ (iii) advanced competency in the local treasury examination and certification system for local treasurers; (iv) an electronic compendium of DOF and BLGF rulings, issuances, and policy guidance; and (v) implementation of the PFM assessment tool for all LGUs.²⁷ These competency assessment tools boost career advancement in local civil services and directly benefit local treasurers and budget officers, of whom 50% are female.

17. **Reform area 3: Improving the local government unit financing and investment framework.** This reform area eases fiscal constraints on local service delivery. The accomplishments under subprogram 1 included the Ease of Doing Business Act and regulations for localized parametric disaster risk insurance. Subprogram 2 continued to expand LGU access to private sector and disaster risk financing and to create a conducive business environment for local development. First, the BLGF finalized and submitted the House Bill on Mandatory Calamity Insurance to the Congress, which requires all LGUs to insure their assets. Second, the DILG completed the LGU Resilience Readiness Monitoring Framework assessment in 40 pilot LGUs in 2020.²⁸ The use of a results-based performance tool helped to fill capacity gaps in disaster risk reduction and management through better local planning and budgeting. Third, the PPP Center issued regulations to expand the scope of the PDMF to help LGUs pursue PPP projects through joint ventures pursuant to the local PPP Code or joint venture ordinance of the LGUs. Fourth, the PPP Center rolled out the Business Case Initiative to help LGUs develop robust business cases for small-scale local PPP projects, with consideration of gender and social safeguards, climate resilience, and gender-responsive policies and guidelines. Fifth, the government rationalized setting local fees and charges across LGUs on a cost-recovery basis, and rolled out an electronic single-service window—the Business One-Stop Shop—to reduce the cost of doing business and speed up the issuance of business permits.²⁹ Sixth, the government enhanced the Rate-My-LGU Service, an online LGU client rating system, with gender monitoring and reporting to encourage citizen feedback and to incentivize LGUs to be more responsive to gender-specific needs. Last, the BLGF developed an online public fiscal reporting dashboard and local tax calculator to increase transparency and accountability of LGUs.

18. **Sustainability and post-program partnership framework.** The post-program partnership framework reflects the government’s commitment to sustaining accomplishments in

²⁶ The competency assessment comprises three components: (i) competency modeling for local budget officers, (ii) the e-Competency Assessment Tool, and (iii) competency assessment of local budget officers.

²⁷ As of December 2019, 1,359 out of a total of 1,715 LGUs had completed the PFM tool, with an average score of 2.97 and with 54% of LGUs assessed as satisfactory (score of 3.0 or higher). Internal and external audit was the most lagging indicator.

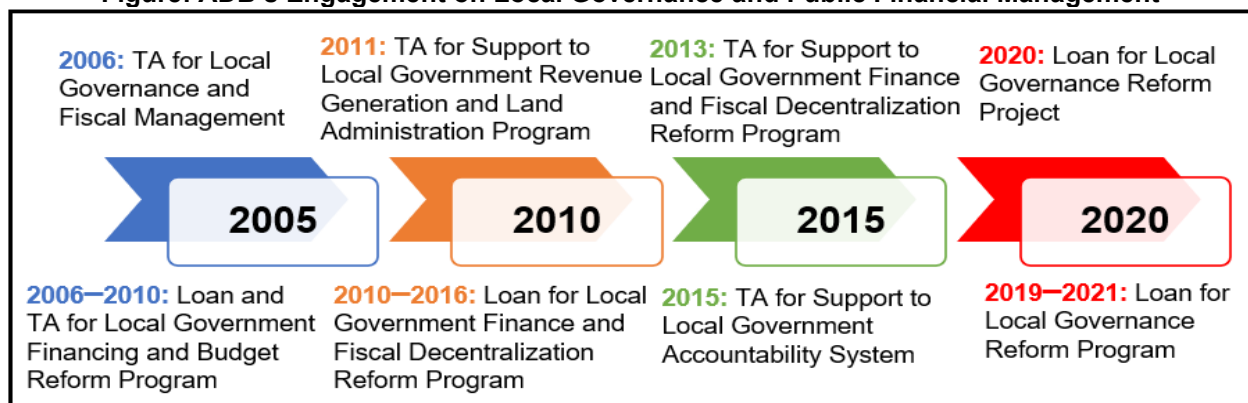
²⁸ Based on the results of the 40 pilot LGUs in 2020, the LGU Resilience Readiness Monitoring Framework mean score was 0.352 or lower, with a range from 0.227 (low) to 0.575 (moderate).

²⁹ BLGF Memorandum Circular 20 (September 2019) provides the guidelines for setting local fees and charges.

all three reform areas. The measures to ensure sustainability include: (i) developing LGUs' transition plans and an equalization mechanism for the full devolution of public services; (ii) providing technical advice and capacity building for effective implementation of the property valuation office; (iii) designing and piloting land value capture mechanisms to supplement the real property valuation reform, and encouraging private sector participation in local infrastructure; (iv) establishing the master plan for the Local Government Academy for LGUs to sustain the capacity building being provided to local treasurers and budget officers; and (v) strengthening LGU capacity to develop pro-poor, pro-women local investments, including social protection projects.³⁰ The measures may lead to a new program to support devolved public services, good local governance, and local revenue mobilization.

19. **ADB's past engagement.** ADB has been a key long-term partner for local governance reform in the Philippines, providing programmatic lending, project investment, and technical assistance. In 2006–2010, the Local Government Financing and Budget Reform Program strengthened the capacity of LGUs to deliver services in line with the 1991 LGC.³¹ In 2010–2016, the Local Government Finance and Fiscal Decentralization Reform Program sustained the thrust of local governance reforms by focusing on the financial capacity of LGUs to fund improved service delivery.³² Subsequently, the program stepped up these reforms by focusing on the quality and efficiency of service delivery under existing structures, while equipping LGUs with the tools, skills, and incentives to better perform their roles. The Local Governance Reform Project (footnote 3) approved in 2020 has helped the BLGF develop the property valuation and transaction database system which strengthened and modernized the functions of the property valuation office accomplished under subprogram 2.

Figure: ADB's Engagement on Local Governance and Public Financial Management



ADB = Asian Development Bank, TA = technical assistance.

Source: Asian Development Bank.

20. **Lessons.** ADB's experience provided five key lessons that have been incorporated into subprogram 2. First, decentralization requires long-term efforts and is sustainable when LGUs align their local priorities with national development plans and the SDGs. Such linkage provides

³⁰ The post-program partnership framework will be financed by ADB's technical assistance (ADB. 2019. [Technical Assistance for Southeast Asia Public Management, Financial Sector, and Trade Policy Facility](#). Manila) and direct charge under ADB's Domestic Resource Mobilization Trust Fund.

³¹ ADB. 2007. [Report and Recommendation of the President to the Board of Directors: Proposed Program Loan and Technical Assistance Grant to the Republic of the Philippines for the Local Government Financing and Budget Reform Program Cluster \(Subprogram 1\)](#). Manila.

³² ADB. 2014. [Report and Recommendation of the President to the Board of Directors: Proposed Programmatic Approach and Policy-Based Loan for Subprogram 1 to the Republic of the Philippines for the Local Government Finance and Fiscal Decentralization Reform Program](#). Manila.

an overarching reform framework to sustain high-level government commitments. Second, changes in tools and regulations must be accompanied with measures to provide local incentives and the ability to gauge performance against a well-defined set of standards to maximize impact. Third, local governance reform should be supplemented with project investment to help LGUs improve PFM.³³ Fourth, local governance reform is successful when backed by the inclusive participation of community members. Participation of women and marginalized groups can be strengthened if local planning and service delivery are carried out in a gender-sensitive manner. Finally, public communications and stakeholders' engagement are essential for successful local governance reform. Under subprogram 2, ADB supported the government for the consultative processes with LGUs, local communities, the civil society organizations, the Philippine Commission on Women, and other stakeholders of the reforms.³⁴

21. ADB's value addition to program design and implementation. ADB's long-term engagement and structured policy dialogue with the government, encompassing all three reform areas, helped prioritize and strengthen legal, policy, regulatory, and institutional reforms. For reform area 1, ADB supported the transition plans needed to prepare national government agencies and LGUs for the devolution of public services by 2022. ADB helped to strengthen local capacity to mainstream gender development in planning and budgeting, and to align them with national plans and the SDGs.³⁵ ADB project developed the property tax valuation database and transaction systems and is professionalizing local assessors (footnote 3).³⁶ For reform area 2, ADB's technical assistance helped develop the e-learning system and the curriculum to build the core competencies of local treasurers, leading to an increase in the number of treasurers who passed the Competency on Local Treasury Examination to 1,403 in 2019 from 577 in 2017.³⁷ For reform area 3, ADB's technical assistance financed by the Urban Climate Change Resilience Trust Fund enabled the PPP Center to form a panel of project development consultants to prepare local PPP projects and ensure project compliance with social and gender safeguards.³⁸

22. Development partner coordination. The government leads development partner coordination in the areas of decentralization and devolution of public services. The Coordinating Committee on Decentralization, chaired by the DILG, acts as secretariat of the Oversight Committee on Devolution, and includes members from government agencies and the leagues of local governments. The committee invites development partners, including ADB; technical staff from Congress; and representatives from civil society organizations. ADB closely coordinated with Agence Française de Développement to implement the LGU Resilience Readiness Monitoring Framework. ADB had regular dialogue with the governments of Australia and Canada on support for local PPP project development and with the United States Agency for International Development for local development in Mindanao. ADB liaised with the International Monetary

³³ ADB. 2018. [Policy-Based Lending 2008–2017: Performance, Results, and Issues of Design](#). Manila.

³⁴ For example, ADB supported the Department of Budget Management to ensure that the Executive Order Number 138 and its potential impacts are well communicated with and supported by LGUs, communities, and civil society organizations. ADB's in-depth assessment of the revenue impacts from the RPVAR also served as inputs for BLGF to formulate its public communications strategies for RPVAR.

³⁵ ADB. 2015. [Technical Assistance to the Republic of the Philippines for Support to Local Government Accountability Systems](#). Manila.

³⁶ Under ADB's project loan and associated technical assistance, a project management unit has been established, and procurement of real property valuation database and transaction systems is ongoing and on track. ADB. 2016. [Technical Assistance to the Republic of the Philippines for Strengthening Tax and Fiscal Policy Capacity for Inclusive Growth](#). Manila.

³⁷ ADB. 2019. [Technical Assistance for Southeast Asia Public Management, Financial Sector, and Trade Policy Facility](#). Manila.

³⁸ ADB. 2011. [Technical Assistance to the Republic of the Philippines for Strengthening Public–Private Partnerships in the Philippines](#). Manila.

Fund and the World Bank to ensure alignment of macroeconomic and fiscal assessment.³⁹

C. Expected Outcome of the Reforms

23. The program is aligned with the Philippines' overarching development objective of enhancing the efficiency, effectiveness, and equity of public service delivery (footnote 16). The program outcome is improved service delivery ability and local governance performance of LGUs.⁴⁰ One of the program's three original outcome indicators has been achieved earlier than was envisaged in subprogram 1: As of December 2019, the number of LGUs with improved SGLG certification totaled 442, or 26% of all LGUs, exceeding the original target of 20% by 2024. Hence, the target has been revised upward to at least 50% and advanced to 2022. The program is on track to achieve the other two original outcome indicators by 2022. Out of all the LGUs, 51.2% prepared and submitted GAD plans and budgets for FY2020, close to the original target of 54%; therefore, the target has been upgraded to 70% by FY2022. Finally, the program has contributed to increased locally sourced revenues of ₱253.7 billion (\$5.2 billion) in FY2019, up by 22.6% from ₱206.9 billion (\$4.3 billion) in FY2017. Subprogram 2 includes nine additional outcome indicators to measure LGUs' budget performance, gender responsiveness, and service delivery for each of the three reform areas. The program impact assessment estimates the economic and social benefits at \$1.4 billion–\$2.5 billion in terms of (i) efficiency gains on local public spending, and (ii) reduced costs of doing business.⁴¹

D. Development Financing Needs and Budget Support

24. The government has requested a regular loan of \$400 million from ADB's ordinary capital resources to help finance subprogram 2.⁴² The loan size is based on the Philippines' larger financing needs, reform impacts, and development spending. For 2021, the government's total gross borrowing requirement is estimated to reach a record high at \$62.3 billion, a significant increase from \$20.1 billion in 2019. Increased borrowing is needed to mitigate the economic impact of the COVID-19 pandemic and to finance the fiscal deficit equivalent to 9.3% of GDP.⁴³ The government plans to raise about \$53.3 billion from the issuance of treasury bills and bonds, \$3.2 billion from official development assistance, and \$5.8 billion from external bonds.⁴⁴

25. The loan will have a 15-year term, including a grace period of 3 years; an annual interest rate determined in accordance with ADB's London interbank offered rate (LIBOR)-based lending facility; a commitment charge of 0.15% per year; and such other terms and conditions set forth in the draft loan agreement. Based on the 30% annuity repayment method, the average maturity is 12.1 years, and there is no maturity premium payable to ADB.

E. Implementation Arrangements

26. The DOF is the executing agency for the program. The BLGF, Department of Budget and Management, the DILG, National Economic and Development Authority, and PPP Center are the

³⁹ Development Coordination (accessible from the list of linked documents in Appendix 2).

⁴⁰ The policy design and monitoring framework is in Appendix 1.

⁴¹ Program Impact Assessment (accessible from the list of linked documents in Appendix 2).

⁴² The loan amount increased from the indicative \$300 million mentioned in the programmatic approach to \$400 million, given the substantial increase in development financing needs.

⁴³ Department of Budget and Management. 2020. *Budget of Expenditures and Sources of Financing 2021*. Manila.

⁴⁴ Subprogram 2 (\$400 million) accounts for 12.5% of the government's planned borrowings from development partners and 0.65% of total gross borrowing requirement in 2021.

implementing agencies. The implementation period is July 2019–June 2021.⁴⁵ A steering committee chaired by the DOF oversees program implementation. The proceeds of the policy-based loan will be withdrawn in accordance with ADB’s *Loan Disbursement Handbook* (2017, as amended from time to time).

III. DUE DILIGENCE

27. **Safeguards.** In compliance with ADB’s Safeguard Policy Statement (2009), the program is classified category C for environment, involuntary resettlement, and indigenous people’s safeguards. The program is not expected to have any adverse environmental or social safeguard impacts within the meaning of ADB’s Safeguard Policy Statement.

28. **Poverty, social, and gender.** Subprogram 2 is categorized as *effective gender mainstreaming*. Key reforms focused on mainstreaming gender spanned across all three reform areas. These reforms included: (i) gender equality goals integrated into the Executive Order on the Full Devolution of LGU Functions; (ii) local planning and budgeting aligned with the national GAD requirement as well as the gender equality SDG (Goal 5); (iii) GAD-PBMS rolled out to strengthen gender mainstreaming in local project development; (iv) GAD monitoring integrated into the LIFT PFM system; (v) SGLG criteria upgraded to incorporate GAD; (vi) capacity development delivered to local treasurers and budget officers (at least 50% female); (vii) the PDMF augmented to target gender and social safeguards and compliance with gender-responsive policies and guidelines in local PPP projects; and (viii) gender monitoring integrated into the Rate-My-LGU Service to incentivize LGUs to meet gender-specific needs of citizens.

29. **Governance.** The 2016 Public Expenditure and Financial Accountability assessment pointed to the soundness and improvement of PFM and fiduciary arrangements of the government, especially policy-based budgeting, transparency, and asset–liability management.⁴⁶ The government took a strategic view of the 2016 Public Expenditure and Financial Accountability findings to improve PFM. The government shifted from an obligation-based to a cash-based budgeting system in 2019. The cash-based budgeting system is based on annual cash payments for contractual obligations in a fiscal year, aiming to incentivize government agencies to be more proactive in budget planning and costing, and more timely in procurement and implementation. The government launched the Budget and Treasury Management System in 2019 to integrate all essential PFM functions across relevant government agencies into a consolidated database. Upon the President’s approval of the National Expenditure Program, the government introduced the early procurement policy, which allows government agencies to undertake advance procurement activities up to the issuance of the notice of award. This policy helped mitigate delays in project implementation associated with delayed procurement.

30. **Risk and mitigating measures.** The overall risk for the program is *moderate*. Major risk and mitigating measure are summarized in Table 1 and described in the risk assessment and risk management plan.

Table 1: Summary of Risks and Mitigating Measures

Risks	Mitigation Measures
COVID-19’s impacts worsen the quality of public service delivery, poverty, and unemployment in local communities,	The government has stepped up local governance reform as part of the COVID-19 economic recovery. Under Republic Act 11494 (Bayanihan to Recover As One Act), the

⁴⁵ List of Ineligible Items (accessible from the list of linked documents in Appendix 2).

⁴⁶ Public Expenditure and Financial Accountability Secretariat. 2016. *Republic of the Philippines PFM Strategy Implementation Support: Public Financial Management and Accountability Assessment*. Washington, DC.

Risks	Mitigation Measures
rendering local governance reforms ineffective.	government allocated ₱1.5 billion (\$31 million) for the Local Government Support Fund for COVID-19 relief efforts in 2020–2021.
Limited absorptive capacity among some LGUs may hamper effective implementation of local governance reforms.	With ADB TA support, the government has prepared transition plans for LGUs (including organizational plans and staffing requirements) to support the full devolution of public services, with continued training of LGU staff. The Master Plan for the Local Government Academy is being developed to support the medium to long-term capacity development of LGU staff.
Limited governance and transparency of public expenditures dilute effectiveness of local public service delivery.	PFM in general is being improved through a series of measures to promote transparency and accountability, with ADB and other development partner support. Powers to approve the schedule market value of real properties are vested with the national government. The Cabinet Cluster on Good Governance and Anti-Corruption has implemented a comprehensive and results-based anticorruption action plan, drawing on a review of the National Anti-Corruption Plan of Action. These initiatives are being supported by various development partners.

ADB = Asian Development Bank, COVID-19 = coronavirus disease, LGU = local government unit, PFM = public financial management, TA = technical assistance.

Source: Asian Development Bank.

31. ADB's Anticorruption Policy (1998, as amended to date) was explained to and discussed with the government.

IV. ASSURANCES

32. The government has assured ADB that implementation of the program shall conform to all applicable ADB policies, including those concerning anticorruption measures, safeguards, gender, procurement, consulting services, and disbursement, as described in detail in the loan agreement.

V. RECOMMENDATION

33. I am satisfied that the proposed policy-based loan would comply with the Articles of Agreement of the Asian Development Bank (ADB) and recommend that the Board approve the loan of \$400,000,000 to the Republic of the Philippines for subprogram 2 of the Local Governance Reform Program, from ADB's ordinary capital resources, in regular terms, with interest to be determined in accordance with ADB's London interbank offered rate (LIBOR)-based lending facility; for a term of 15 years, including a grace period of 3 years; and such other terms and conditions as are substantially in accordance with those set forth in the draft loan agreement presented to the Board.

Masatsugu Asakawa
President

4 August 2021

POLICY DESIGN AND MONITORING FRAMEWORK

Country's Overarching Development Objective Efficient, effective, and equitable public service delivery enhanced (Updated Philippine Development Plan, 2017–2022) ^a			
Outcome Service delivery ability and local governance performance of LGUs improved		Risks and Critical Assumptions R: COVID-19's impacts worsen the quality of public service delivery, poverty, and unemployment in local communities, rendering local governance reforms ineffective	
Prior Actions: Subprogram 1 Completed June 2017–June 2019	Prior Actions: Subprogram 2 Completed July 2019–June 2021	Outcome Indicators^b	Post-Program Partnership Framework
Reform area 1: Strengthening the local governance framework for service delivery			
<p>1. To improve local service delivery, the government submitted a suite of amendments to the 1991 LGC for congressional approval to strengthen the framework for central–local relations. Measures include (i) clarification of functional and expenditure assignments across national and subnational levels of government; (ii) promotion of inter-LGU cooperation for service delivery agreements; and (iii) updated income requirements for creation of municipalities, provinces, and highly urbanized cities. (DILG)</p> <p>2. To strengthen the legal framework for local revenue mobilization, the government submitted amendments to the 1991 LGC for congressional approval. Amendments include (i) rebalancing the share of business tax revenue collected based on location of activity; (ii) increasing local autonomy in the use of natural resource revenues; (iii) limiting central and local government power to issue tax exemptions for LGUs; (iv)</p>	<p>1. To strengthen the greater roles of LGUs in reducing poverty, promoting gender equality and human capital development, and pursuing peace and order, the government (i) incorporated the increased IRA for LGUs in the 2022 national budget preparation in line with the Mandanas ruling and clearer delineation of national and local government roles, and (ii) approved the Executive Order on the Full Devolution of Functions to LGUs to institute a legal framework for implementation of the Mandanas ruling and transition plans. (DBM)</p>	<p>By 2022:</p> <p>a. At least 70% of total LGUs (provinces, cities, and municipalities) submit their 2022 GAD plans and budgets to the DILG in compliance with SGLG requirements.^c (2018 baseline: 37%; 2019 actual: 51.2%) Source: DILG's SGLG Database</p> <p>b. Total own-source LGU revenues increased by 30% in nominal terms over the 2017 baseline (2017 baseline: ₱206.9 billion; 2019 actual: ₱253.7 billion) Source: BLGF e-SRE reports</p> <p>c. LGUs' expenditure on GAD projects as a percentage of total national budget increased to at least 6% of total national budget (2018 baseline: 5.1%) Source: COA Gender and</p>	<p>1. National government agencies' transition plans and equalization mechanism (including organizational plans and staffing requirements) for the full devolution of public services are supported and prepared. (DBM) (TA 9766-REG)^d</p>

Prior Actions: Subprogram 1 Completed June 2017–June 2019	Prior Actions: Subprogram 2 Completed July 2019–June 2021	Outcome Indicators^b	Post-Program Partnership Framework
<p>improving consistency of rate setting for local fees and charges; and (v) institutionalizing local PFM, including gender-responsive budgeting. (DILG)</p> <p>3. To support a national priority policy for increasing LGU own-source revenue, the House of Representatives passed, on third reading, the Real Property Valuation and Assessment Reform Act. (BLGF)</p> <p>4. To strengthen accountability of local service delivery, the government facilitated linking LGU planning to annual budgets by requiring the submission of the CDP and LDIP as documentary requirements for the</p>	<p>2. To accelerate implementation of the real property valuation reform, the government: (i) set up the property valuation office at the BLGF, and (ii) established the BLGF Management Committee to oversee overall implementation of the Real Property Valuation and Assessment Reform and to provide technical and policy advice as well as coordination support to the DOF and concerned agencies to ensure success of the reform. (BLGF)</p> <p>3. To enable the national government to track and report local government planning and budgeting and to mainstream gender perspectives in local government plans, the government rolled out an online system for real-time submission and tracking of the LDIP and adopted the use of the GAD plan budget monitoring system. (DILG with support from DBM)</p> <p>4. To align national strategies and plans with local priorities for service delivery, the government strengthened local planning and budgeting frameworks for LGUs to identify priority and devolved</p>	<p>Development Accomplishment Reports</p> <p>d. Budget execution rates among LGUs improved to at least 85% of total budget (2018 baseline: 72.2% of total budget) Source: COA Annual Financial Reports</p>	<p>2. Technical advice and capacity building of local assessors continue to be provided to BLGF to fully operationalize the property valuation office. (TA 9766-REG)^d</p> <p>3. Land value capture mechanisms are developed and piloted in selected local transit-oriented development projects, such as Metro Rail Transit stations and bus terminals, to supplement real property valuation reform and encourage private sector participation in local infrastructure projects. (BLGF) (ADB's Domestic Resource Mobilization Trust Fund)</p> <p>4. Training programs continue to be conducted for BLGF regional offices, with emphasis on increased revenue collection and local</p>

Prior Actions: Subprogram 1 Completed June 2017–June 2019	Prior Actions: Subprogram 2 Completed July 2019–June 2021	Outcome Indicators^b	Post-Program Partnership Framework
<p>SGLG. (DILG)</p> <p>5. To strengthen responsiveness of local service delivery, the government linked LGU plans and investment programs in the CDP and LDIP with the PDP and strengthened the role of Regional Development Councils. (DILG)</p>	<p>projects in the LDIP and align them with the PDP and Philippine Investment Program, 2017–2022; the Philippine Plan for Gender-Responsive Development, 1995–2025; and the Sustainable Development Goals. (DBM and DILG)</p> <p>5. To enhance local PFM capacity among LGUs, the government streamlined revenue mobilization and budget functions of LGUs and regional government offices, and improved existing guidelines and manuals for local PFM, including issuance of (i) the updated policy for Model Local Revenue Code, (ii) the updated Local Treasury Operations Manual, and (iii) the updated guidelines on the assessment of Comprehensive Development Plan of cities and municipalities. (BLGF, DBM, and DILG)</p>		<p>budgeting and planning, including gender mainstreaming in LDIP and GAD budget and plan. (BLGF) (TA 9766-REG)^d</p>
Reform area 2: Modernizing and professionalizing local public financial management			
<p>6. To address weaknesses in the accuracy, integrity, timeliness, and accountability in subnational financial reporting, the government designed and operationalized the LIFT PFM system in all LGUs, standardizing fiscal reporting and consolidating subnational financial accounts. (BLGF)</p>	<p>6. To improve efficiency, transparency, and oversight of local budget planning and utilization, the government linked the enhanced LGU e-Budget Preparation Module with the BLGF and DILG systems and included monitoring of GAD projects. (BLGF and DBM)</p>	<p>By 2022:</p> <p>e. At least 50% of total LGUs (provinces, cities, and municipalities) pass the enhanced SGLG criteria including GAD budget and plan^e (2018 baseline: 15%; 2019 actual: 26%) Source: DILG's List of the SGLG Awardees</p>	<p>5. GAD databases for LGUs are developed to supplement the integration of GAD coding in the LGU e-Budget preparation module. (DBM) (TA 9766-REG)^d</p>

Prior Actions: Subprogram 1 Completed June 2017–June 2019	Prior Actions: Subprogram 2 Completed July 2019–June 2021	Outcome Indicators^b	Post-Program Partnership Framework
<p>7. To strengthen the capacity and professionalize the local treasury service, the government designed and operationalized the Standardized Examination and Assessment for Local Treasury Service program. (BLGF)</p>	<p>7. To promote gender and social protection development and address service delivery gaps for women and vulnerable groups such as children, elderly, and persons with disabilities, the government introduced the minimum PFM performance standards for the SGLG, through inclusion of additional PFM criteria in the implementing rules and regulations, including fiscal sustainability of LGUs and increased spending on priority sectors such as social protection, health, and education. (BLGF, DBM, and DILG)</p> <p>8. To further improve the capacities of the local treasury service, the government designed and developed an e-learning capacity development platform to build core competencies for treasurers. (BLGF)</p> <p>9. To strengthen the capacity and professionalize the local budget officers, the government launched a competency measurement and assessment system for Local Budget Officers.^f (DBM)</p> <p>10. To complete the professionalization of the local treasury service, the government rolled out the Advanced Competency in Local Treasury Examination and Certification System for Local Treasurers.^g (BLGF)</p>	<p>f. At least 400 local treasurers and LGU staff (of whom at least 50% are female) pass the Advanced or Intermediate Competency in Local Treasury Examination and Certification System for Local Treasurers. (2020 baseline: 57) Source: BLGF reports.</p> <p>g. The average PFMAT scores of all LGUs improved to at least 3.2 out of 5. (2019 baseline: 2.97) Source: DBM reports.</p>	<p>6. A master plan for the capacity development of LGUs by the Local Government Academy is developed and implemented in compliance with the enhanced SGLG criteria, for medium- to long-term professionalization of local treasurers, budget officers, and LGU staff and units. (DBM and DILG) (TA 9766-REG)^d</p>

Prior Actions: Subprogram 1 Completed June 2017–June 2019	Prior Actions: Subprogram 2 Completed July 2019–June 2021	Outcome Indicators^b	Post-Program Partnership Framework
8. To guide and strengthen LGU PFM, the government resolved inconsistencies and developed a consolidated database for DOF rulings, issuances, and policy guidance covering the years 1993–2017. (BLGF) 9. To emphasize the national government intent to recognize and reward good performance in local PFM and service delivery, DOF has made the LGU Fiscal Sustainability Scorecard a national policy. (BLGF)	11. To guide and strengthen LGU PFM, the government rolled out an electronic compendium of DOF and BLGF rulings, issuances, and policy guidance. (BLGF) 12. To improve monitoring of local PFM performance, the government completed the PFMAT for all LGUs and required LGUs to undertake the PFMAT every three years. (DBM)		
Reform area 3: Improving the local government unit financing and investment framework			
10. To improve LGU access to credit financing, the government submitted amendments to the LGC for congressional review, introducing a local financing and debt framework and fiscal rules to improve creditworthiness of LGUs. (DILG) 11. To strengthen resilience of LGUs and improve disaster risk preparedness, the government introduced a new parametric insurance modality. (DOF)	13. To enhance community resilience against natural hazard events and strengthen disaster risk financing of LGUs, the government submitted the House Bill on Mandatory Calamity Insurance to the Congress, which mandates all LGUs to insure their assets. (BLGF) 14. To strengthen the use of LGU result-based performance in disaster risk reduction management and address capacity gaps among LGUs, the government assessed LGU capacity with the application of the LGU Resilience Readiness Monitoring Framework and Tool and integrated the assessment results into the local planning and budgeting process. (DILG)	By 2022: h. At least 75% of total LGUs (provinces, cities, and municipalities) have the calamity insurance for public assets. (2020 baseline: 32.5% of all LGUs have calamity insurance for public assets) Source: DILG reports. i. LGU Resilience Readiness Index improved (2020 baseline: 0.352 out of 1.0) Source: DILG’s LGU Resilience Readiness Reports. j. At least 15 local PPP projects supported by the PPP Center in the	7. LGUs’ PPP projects are further developed to strengthen pro-poor, pro-women investment, including social protection projects. (PPP Center) (TA9766-REG) ^d

Prior Actions: Subprogram 1 Completed June 2017–June 2019	Prior Actions: Subprogram 2 Completed July 2019–June 2021	Outcome Indicators^b	Post-Program Partnership Framework
<p>12. To strengthen disaster performance assessment systems, the government introduced the LGU Resilience Readiness Monitoring Framework, enhanced from the Disaster Preparedness Assessment System, to more effectively measure and encourage LGUs' recalibration of efforts from disaster preparedness to resilience. (DILG)</p> <p>13. To enhance LGU access to nontraditional private financing, the government extended access of an advisory panel of experts, including women advisors, and established knowledge centers in NEDA regional offices. (PPP Center, NEDA)</p> <p>14. To improve efficiency in the delivery of public services and reduce the cost of doing business, the government enacted the Ease of Doing Business Act for red-tape reduction and fast-tracking and streamlining of business permit and licensing issuance across all levels of government, including publication of a citizen's charter in local dialect to inform all citizens of the act. (DILG)</p>	<p>15. To enhance LGU capacities to develop PPP projects, the government issued the regulations to expand the scope of the PDMF to support local PPP projects through joint ventures. (PPP Center)</p> <p>16. To enhance LGU capacities to develop PPP projects, the government rolled out the Business Case Initiative to assist LGUs with developing their robust business cases for small-scale local PPP projects, with due consideration of gender and social safeguards, climate resilience, and gender-responsive policies and guidelines. (PPP Center)</p> <p>17. To further reduce the cost of doing business and improve timeliness in business permit issuance, the government consolidated local licensing and permit issuances and rationalized setting of fees and charges for the Business One-Stop Shop on a cost-recovery basis. (DILG)</p> <p>18. To encourage citizen feedback, and to inform LGU policies and interventions and incentivize LGUs to be more responsive to gender-specific needs, the government</p>	<p>development, evaluation, and/or procurement stages, including the Business Case Initiative and funding support under the PDMF, with resiliency measures and environmental, gender, and social safeguards (2020 baseline: 5 local PPP projects supported) Source: PPP Center reports.</p> <p>k. All LGUs complied with the required processing time under the Ease of Doing Business Act (i.e., 3 working days for simple transactions, 7 working days for complex transactions, and 20 working days for highly technical transactions). (2020 baseline: 92%) Source: DILG reports.</p> <p>i. At least 80% of LGUs implemented gender tracking and reporting of female respondents to the Rate-My-LGU Service. (2020 baseline: 40%) Source: DILG reports.</p>	<p>8. Business Processing and Licensing Office Operations Manual is developed to streamline service standards of the Business One-Stop Shop, with regular reporting and monitoring of the Rate-My-LGU Service and Citizen Satisfaction Index System. (DILG) (TA 9766-REG)^d</p>

Prior Actions: Subprogram 1 Completed June 2017–June 2019	Prior Actions: Subprogram 2 Completed July 2019–June 2021	Outcome Indicators ^b	Post-Program Partnership Framework
<p>15. To enhance LGU performance and citizen feedback on local service delivery, the government has developed and operationalized an online LGU client rating system for business permit application and releasing. (DILG)</p>	<p>19. To improve transparency and accountability of LGUs, the government enhanced public access to LGUs’ fiscal and financial information as well as local tax information by developing an online public fiscal reporting dashboard and local tax calculator^h (BLGF)</p>		

Budget Support
 ADB: \$300,000,000 (loan for subprogram 1)
 ADB: \$400,000,000 (loan for subprogram 2)

ADB = Asian Development Bank, BLGF = Bureau of Local Government Finance, CDP = Comprehensive Development Plan, COA = Commission on Audit, COVID-19 = coronavirus disease, DBM = Department of Budget and Management, DILG = Department of the Interior and Local Government, DOF = Department of Finance, e-SRE = electronic statement of receipts and expenditures, GAD = gender and development, IRA = internal revenue allotments, LDIP = Local Development Investment Program, LGC = Local Government Code, LGU = local government unit, LIFT = LGU Integrated Financial Tool, NEDA = National Economic and Development Authority, PDMF = Project Development and Monitoring Facility, PDP = Philippine Development Plan, PFM = public financial management, PFMAT = public financial management tool, PPP = public–private partnership, R = risks, REG = regional, SGLG = Seal of Good Local Governance, TA = technical assistance.

^a National Economic and Development Authority. 2021. *Updated Philippine Development Plan, 2017–2022*. Manila.

^b Outcome indicators may cover multiple reform areas.

^c The target was revised upward to “at least 70%” and advanced to 2022, from “54% by 2024”.

^d ADB. 2019. *Technical Assistance for the Southeast Asia Public Management, Financial Sector, and Trade Policy Facility*. Manila.

^e The target was revised upward to “at least 50%” and advanced to 2022, from “20% by 2024”.

^f The local budget officer competency measurement and assessment system comprises four clusters: (i) maintenance of PFM understanding; (ii) application of internal control; (iii) use of information technology to manage finances; and (iv) effective collaboration.

^g The Advanced Competency in Local Treasury Examination and Certification System for Local Treasurers covers the following: (i) leading change in organizations, (ii) improvement and innovations in work-productivity and quality, (iii) advanced data analytics, (iv) advanced risk management and internal control system, (v) information management and communication strategies, (vi) public policy review and development, and (vii) evolution of PFM practices.

^h The online public fiscal reporting dashboard of the Local Government Financial Performance System tracks the fiscal performance of LGUs. The local tax calculator is an interactive dashboard which allows the public to access business tax, real property tax, and community tax charges.

Contribution to Strategy 2030 Operational Priorities: Operational priority indicators to which this operation will contribute results are detailed in Contribution to Strategy 2030 Operational Priorities (accessible from the list of linked documents in Appendix 2).

Source: Asian Development Bank.

LIST OF LINKED DOCUMENTS

<http://www.adb.org/Documents/RRPs/?id=52173-003-3>

1. Loan Agreement
2. Sector Assessment (Summary): Public Sector Management
3. Contribution to Strategy 2030 Operational Priorities
4. Development Coordination
5. International Monetary Fund Assessment Letter
6. Summary Poverty Reduction and Social Strategy
7. Program Impact Assessment
8. Risk Assessment and Risk Management Plan
9. List of Ineligible Items
10. Approved Report and Recommendation of the President to the Board of Directors: Proposed Programmatic Approach and Policy-Based Loan for Subprogram 1 to the Republic of the Philippines for Local Governance Reform Program

Supplementary Documents

11. Country Economic Indicators
12. Climate Change Assessment
13. Public Financial Management Assessment
14. Comparison of Original and Revised Subprogram 2

DEVELOPMENT POLICY LETTER

Republic of the Philippines
DEPARTMENT OF FINANCE
 Roxas Boulevard Corner Pablo Ocampo, Sr. Street
 Manila 1004

DEVELOPMENT POLICY LETTER

MR. MASATSUGU ASAKAWA
 President
 Asian Development Bank (ADB)
 Manila, Philippines



Dear **President ASAKAWA**,

On behalf of the Government of the Republic of the Philippines (Government), we would like to express our appreciation for the continuous commitment and support of the Asian Development Bank (ADB) towards local governance reform and fiscal decentralization. This development policy letter highlights the Government's commitment to improving local governance and fiscal decentralization as the impetus for a people-centered, efficient, and equitable public service delivery to achieve the Sustainable Development Goals (SDGs), in line with the Philippine Development Plan (PDP) 2017-2022.

The Philippines sustained strong growth averaging 6.4% in 2015-2019, with consistent poverty reduction from 21.6% in 2015 to 16.6% in 2018. However, our economy was hard hit by the coronavirus disease (COVID-19). LGUs are at the forefront of meeting local demand for critical public services such as health care, social assistance, and livelihood support. Moreover, following the Supreme Court Decision dated 10 June 2019 ("Mandanasruling"), LGUs will have greater access to funds for devolved services from fiscal year (FY) 2022 onwards. Given these emerging needs and developments, we envisage that local governance reforms will play an ever-increasing role in putting in place a sustainable economic recovery and realizing full devolution of public services.

To sustain the momentum achieved under Subprogram 1 of the Local Governance Reform Program (LGRP), we have identified key reforms to be supported under Subprogram 2 covering the period July 2019 to May 2021. The USD400 million loan will allow the Government to meet its development financing needs in FY 2021, which is estimated to reach a record high at \$62.3 billion to address economic impacts of the COVID-19 pandemic.

Strengthening the local governance framework for service delivery

The Government has moved towards the full devolution of public services and

governments in line with the Mandanas ruling, and the preparation of LGUs for transition toward assuming greater roles in reducing poverty and promoting gender equality and human capital development. In achieving this, the Government incorporated the increased internal revenue allotments (IRA) for LGUs in the 2022 national budget preparation. On the other hand, to institute a legal framework for implementation of the Mandanas ruling and transition plans, the Government approved Executive Order (EO) Number 138 on the Full Devolution of Functions to LGUs on June 1, 2021.

Moreover, under Subprogram 2, the Government operationalized the property valuation office at the Bureau of Local Government Finance (BLGF) and established the BLGF Management Committee to oversee overall implementation of the real property valuation and assessment reform (RPVAR). The Government has also implemented an online system for real-time submission and tracking of the Local Development Investment Program. The local planning and budget frameworks for LGUs were also strengthened by aligning programs, projects, and activities of LGUs with the PDP; the Public Investment Program, 2017-2022; and the SDGs.

Modernizing and professionalizing local public financial management: The Government introduced several critical public financial management (PFM) measures and tools to strengthen LGU capacities to efficiently perform PFM functions. Subprogram 2 continued to improve core public finance functions of LGUs and expand tools and incentives to promote efficient and high-quality delivery of public services. The Government introduced the minimum PFM performance standards for the Seal of Good Local Governance (SGLG). The enhanced SGLG criteria included fiscal sustainability of LGUs and increased spending on priority sectors such as social protection, health, and education. Additionally, the Government introduced five critical capacity development initiatives to professionalize local treasurers and budget officers.

Improving the local government unit financing and investment framework: Building upon reform achievements under Subprogram 1, the Government finalized and submitted the House Bill on Mandatory Calamity Insurance to the Congress under Subprogram 2, which mandates all LGUs to insure their assets. Moreover, the Government piloted the LGU Resilience Readiness Monitoring Framework assessment in 40 LGUs in 2020 and integrated the assessment results into local planning and budgeting.

Under subprogram 2, the Government encouraged LGUs to catalyze private

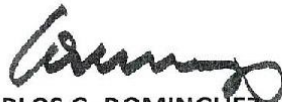


sector participation in local development. Specifically, the Government issued the regulations to expand the scope of the Project Design and Monitoring Facility (PDMF) to include local public-private partnership (PPP) projects through joint ventures. In addition, the Government rolled out the Business Case Initiative recognizing that local PPP projects are small-scale in nature and often have no economies of scale for project preparation under the PDMF.

Following the passage of the Ease of Doing Business Act under Subprogram 1, the Government continued to improve LGU service efficiency, reduce cost of doing business, and enhance the quality and transparency of LGU performance monitoring through an LGU client rating system and rationalization of local fees and charges on a cost-recovery basis. Under Subprogram 2, the Government consolidated the issuance of local licenses and permits under the Business One Stop Shop. In addition, the Government operationalized the enhanced Rate-My-LGU Service with broader coverage and gender monitoring to encourage citizen feedback and incentivize LGUs to be more responsive to gender-specific needs.

In closing, Mr. President, the Government is fully committed to the local governance reform agenda and to implement the reforms already instituted. We look forward to the successful outcomes of LGRP Subprogram 2, and to the continuation of our partnership to meet the Government's vision of fiscal decentralization in the Philippines. Your prompt consideration of this loan will be highly appreciated.

Sincerely,



CARLOS G. DOMINGUEZ
Secretary of Finance

JUN 17 2021

