

[DOF, July 16, 2004]

IMPLEMENTING RULES AND REGULATIONS OF EXECUTIVE ORDER NO. 279, SERIES OF 2004 "PRESCRIBING GUIDELINES ON INSTITUTING REFORMS IN THE FINANCING POLICIES FOR THE WATER SUPPLY AND SEWERAGE SECTOR AND WATER SERVICE PROVIDERS AND PROVIDING FOR THE RATIONALIZATION OF LWUA'S ORGANIZATIONAL STRUCTURE AND OPERATIONS IN SUPPORT THEREOF"

SECTION 1. Purpose - To prescribe the guidelines, criteria, grounds and procedures which shall govern financing policies for the water supply and sewerage sector and the rationalization of LWUA's organizational structure, operation and refocusing of its objectives.

SECTION 2. Coverage - These IRR shall cover all water districts (WDs) other water service providers (WSPs) outside the coverage of MWSS /Maynilad/Manila Water, and all concerned government agencies which have a role in the implementation of EO 279, such as but not limited to the Department of Finance (DOF), National Economic and Development Authority (NEDA), Department of Budget and Management (DBM), Department of Interior and Local Government (DILG), Office of the President (OP), Local Water Utilities Administration (LWUA), Government Financial Institutions (GFIs), Municipal Finance Corporation (MFC), Department of Public Works and Highways (DPWH), Department of Environment and Natural Resources (DENR), Rural Waterworks and Sanitation Associations (RWSAs) and Barangay Waterworks and Sanitation Associations (BWSAs).

SECTION 3. Reforms, Objectives and Policies - In view of the shifts in government financing policies and constraints in the availability of financing from the National Government, there is a need to review and rationalize current financing policies for the Philippine water supply and sewerage sector to allow for the efficient flow of resources to the sector. Cognizant of the need, these IRR hope to address the following reforms, objectives and policies:

- a. Improvement of investor confidence in the water supply and sewerage sector;
- b. Rationalization in the allocation of scarce financial resources in the water supply and sewerage sector through classification and graduation initiatives;
- c. Freedom of choice of WSPs in sourcing financing;
- d. Increase in the participation of LGUs, GFIs, PFIs in the financing of the water supply and sewerage sector;

- e. Stimulation of improved service and creation of financial self-sustainability for WSPs;
- f. Encouragement of initiatives aimed at self-sufficiency of water service providers, including, but not limited to, amalgamation, private sector participation, cost-recovery tariffs, and resource pooling;
- g. Grant of incentives for the improvement and graduation of WSPs; and
- h. Education of consumers towards treating water as a scarce economic good.

SECTION 4. Definition of Terms - For purposes of these IRR, the following terms are defined:

- a. Amalgamation - consolidation, joint operation or annexation of two or more WSPs resulting into a WD.
- b. Classification - categorization of WSPs into non-creditworthy, pre-creditworthy, semi-creditworthy or creditworthy to determine proper allocation of financing.
- c. Cost Recovery Tariff - tariff that is required to cover investment in capital expenditures, operating expenditures and debt servicing, including minimal reserve for collateral or counterpart equity, and reserve for recovery of and some minimal return on LGU's investment/infusion in the WDs or WSPs.
- d. Creditworthy WSPs - financially self-sustaining WSPs capable of accessing financing from GFIs and/or PFIs.
- e. Government Financial Institutions (GFIs) - Development Bank of the Philippines (DBP), Land Bank of the Philippines (LBP) and other financing institutions owned and controlled by the Government.
- f. Graduation - the progression of a WSP from non-creditworthy to pre-creditworthy status or from a pre-creditworthy to semi-creditworthy status and/or from a semi-creditworthy to creditworthy status based on improvements in financial and operational indicators.
- g. Local Government Units (LGUs) - territorial and political subdivisions of the Philippines, consisting of provinces, cities, municipalities and barangays.
- h. Long Term - period covering more than five (5) years.
- i. Medium Term - period covering between three (3) and five (5) years.
- j. Non-Creditworthy WSPs - WSPs with potential to reach pre-creditworthy status in the medium-term, based on relevant financial and operational indicators set by the Oversight Committee.

k. Pre-Creditworthy WSPs - WSPs which are not likely to become creditworthy in the medium-term due to performance issues but can demonstrate the potential for creditworthiness in the long-term, as may be determined based on relevant financial and operational indicators set by the Oversight Committee.

l. Private Financial Institutions (PFIs) - private entities which are primarily organized for the purpose of extending credit facilities to consumers and to industrial or agricultural enterprises. Financing institutions other than government financial institutions. These include universal and commercial banks.

m. Semi-Creditworthy WSPs - WSPs with the demonstrated ability to achieve creditworthiness in the short-term, based on relevant financial and operational indicators set by the Oversight Committee, but either lack the full criteria for creditworthiness or do not meet the criteria consistently.

n. Short Term - period covering one year (1) to less than three (3) years.

o. Technical Assistance - includes feasibility study, detailed engineering design, review of feasibility study and engineering design, preparation of work program, construction supervision, start-up operations, operations and maintenance assistance, rehabilitation of dilapidated systems, well drilling and construction of new wells, rehabilitation and repair of old wells and emergency repair of water supply system. Financing for technical assistance involving pre-feasibility or feasibility studies, project identification, sector survey, institution building activities including training, shall be charged against beneficiaries unless grants are available for the purpose. On the other hand consultancy/advisory services related to construction activities, including detailed engineering shall be considered as part of the project capital cost and may be financed by the project loan.

p. Value Threshold - the level at which LWUA may grant project-related technical assistance for free to the PCW and NCW WSPs without affecting LWUA's viability. This will be determined by the LWUA on a yearly basis depending on LWUA's capability to absorb such additional cost.

q. Water Service Providers (WSPs) - local water utilities such as WDs, LGU-run water utilities, rural waterworks and sanitation associations (RWSAs), and barangay waterworks and sanitation associations (BWSAs), regardless of location.

SECTION 5. Responsibilities - The implementation of the recommended reforms requires that LWUA as the focal government agency for financing and institutional development of local WDs, focuses its objectives and rationalizes its operations. Accordingly, the rationalization of LWUAs organizational structure, operation and refocusing of its objectives, and the implementation of the reforms in the financing policies for the water supply and sewerage sector, as defined in Section 2 of these

IRR, require close policy coordination among the concerned government agencies.

5.1 Local Water Utilities Administration

LWUA, subject to applicable laws and regulations, shall review its organizational structure and internal policies and programs, rationalize its operations and refocus its objectives to include other WSPs, whenever feasible or applicable, to facilitate implementation of and conform with the policies enunciated in EO 279. Further, LWUA shall conduct its operations in a transparent, efficient and effective manner.

LWUA shall constitute and designate from its current organization set-up, a Water Development Group (WDG), a Water Development Financier (WDF) and a Technical Assistance Group (TAG), or similar structures, with functions and responsibilities as follows:

5.1.A Water Development Group (WDG)

WDG shall have the following responsibilities:

- a) It shall be primarily charged with the continuation of LWUA's current institutional development services aimed at graduating WSPs, as well as the classification of WSPs.
- b) It shall classify the WSPs into either creditworthy, semi-creditworthy, pre-creditworthy or non-creditworthy for the purpose of determining the appropriate sources of financing. WSPs initially classified by WDG as creditworthy and/or non-creditworthy shall be subject to further review by the Oversight Committee pursuant to Section 5.2(b) of these IRR.

LWUA shall initially cover the classification and graduation plan and initiatives of WDs. It may also cover other WSPs as deemed applicable or feasible.

To facilitate the classification of the WDs, LWUA shall prepare the criteria for classification and submit the same to the Oversight Committee for review within 30 days upon effectivity of EO 279.

The criteria shall consider:

- i) financial indicators such as current ratio, debt service ratio, debt/equity ratio, profit margin ratio and cash flow ratio; and
- ii) operational indicators such as collection efficiency, non-revenue water and service connections/staff.

LWUA shall closely coordinate with the GFIs in determining the criteria for classification.

The classification of WDs shall be duly approved by the LWUA Administrator for submission to the Oversight Committee for review within 90 days upon completion of review of classification criteria by the OC.

For the initial classification, WDs have to meet the criteria for three (3) consecutive years to be considered creditworthy. WDs classified as semi-creditworthy, pre-creditworthy and non-creditworthy shall be subject to periodic review by WDG at least once every three (3) years for purposes of reclassification. In like manner, subsequent classification shall require three (3) years consistent favorable evaluation. At their own instance, WDs may request the WDG for an annual reclassification review.

Any changes in the classification should be submitted to the Oversight Committee.

Lending to WDs initially classified as creditworthy shall be governed by Section 9 (b) of these IRR.

c) It shall develop a graduation plan for non-creditworthy, pre-creditworthy and semi-creditworthy WSPs based on the following graduation initiatives:

i) Cost Recovery Tariff Initiatives - these are initiatives aimed at achieving widespread full cost recovery tariffs in the long-term. The initiatives shall include the inventory of non-creditworthy, semi-creditworthy and pre-creditworthy WSPs to determine the degree to which tariffs are sufficient to accumulate at least a minimal reserve for collateral or counterpart equity. In addition, should the LGUs invest in WSPs, they should be allowed recovery of and some minimal return on their investment.

ii) Amalgamation and Private Sector Participation Initiatives - these are initiatives aimed at achieving economies of scale and efficiency of service through the use of identified amalgamation and private sector participation techniques based on technical, geographical, economic and other indicators.

LWUA shall formulate within 180 days upon effectivity of these IRR, the necessary guidelines to be observed by the amalgamated WSPs during the transition period. Among other things, the guidelines shall address the a) incentives for amalgamation, b) mechanics of amalgamation, c) restructuring of the Board of Directors and officers of the amalgamated WSPs with respect but not limited to, tenure of office and surviving positions, and d) controlling WSPs taking into account considerations such as the size, financial condition and the location of the participating WSPs.

iii) Management Structure and Governance - These initiatives pertain to institutional improvements within the WSPs' structure leading to greater accountability and improved service.

iv) LGU/WSP Resource Coordination for Credit Enhancement - this refers to the pooling of resources between semi-creditworthy and/or pre-creditworthy and/or non-creditworthy WSPs and the relevant LGUs in their service areas to finance water supply and sewerage projects or create the collateral needed to borrow from GFIs and PFIs.