

SAFE AND CLEAN WATER FOR THE POOR AND BY THE POOR



**MDGIF**

MDG ACHIEVEMENT FUND IN THE PHILIPPINES

# Incentive Mechanisms and Partnership Modalities for Water Supply Provision for the Poor



**December 2011**



SAFE AND CLEAN WATER FOR THE POOR AND BY THE POOR



MDG ACHIEVEMENT FUND IN THE PHILIPPINES

MDG-F 1919:

Enhancing Access to and Provision of Water  
Services with the Active Participation of the Poor

# **Incentive Mechanisms and Partnership Modalities**

DECEMBER 2011





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## ABOUT THE MDG-F 1919

### Joint Programme on Enhancing Access to and Provision of Water Services with the Active Participation of the Poor

The MDG-F 1919 Joint Programme on Enhancing Access to and Provision of Water Services with the Active Participation of the Poor is jointly implemented by the Philippine Government and United Nations partners to enhance provision of and access to water services by filling the “soft” component gaps of existing national government programs that focus only on infrastructure (“hard” components) provision.

Bringing together the NEDA, DILG, and the NWRB, with UNDP and UNICEF as UN Partners over a three-year period (starting May 2009), the Joint Programme specifically aims to contribute in partially addressing issues in low investments and low capacities by 1) establishing investment support mechanisms to improve efficiency, access, affordability and quality of water; and 2) enhancing capacities at the local level to develop, operate and manage water utilities, to benefit 122,000 households in 36 municipalities in Regions 2, 5, 9, 10, and 13.

OUTPUT	
Outcome 1:	Investment support mechanisms established for poor communities/municipalities to improve efficiency, access, affordability and quality of potable water
Output 1.1	Incentive mechanisms and partnership modalities developed and enhanced for public and private investments in “waterless” and poor communities
Output 1.2:	Financing and programming policies in the sector reviewed and amended as necessary to rationalize assistance and increase ownership and accountability
• Output 1.2.1:	NG-I.GU cost sharing policy reviewed and amended, as necessary
• Output 1.2.2:	P3W programming policies reviewed and amended, as necessary
Output 1.3:	Local WATSAN councils and water user associations organized to effect participative provision of water supply services
Output 1.4:	Adjustment of NWRB’s tariff-setting guidelines for small water service providers
Outcome 2:	Enhanced local capacities to develop, operate and manage water utilities
Output 2.1:	Capacities at the local level strengthened, with participation of marginalized groups especially women.
• Output 2.1.1:	Skills and knowledge transferred/shared through institutionalization of local mentoring mechanisms
• Output 2.1.2:	WATSAN Toolbox rolled out and implemented
Output 2.2:	Improved sector plans formulated and monitoring mechanisms established
Output 2.3:	Localized customer service code developed and adopted



## LIST OF ACRONYMS AND ABBREVIATIONS

<b>BWSA</b>	Barangay Water Supply Association
<b>DILG</b>	Department of the Interior and Local Government
<b>DPWH</b>	Department of Public Works and Highways
<b>DOH</b>	Department of Health
<b>DOF/GFIs</b>	Department of Finance/Government Financial Institutions
<b>DOF/MDFO</b>	Department of Finance/Municipal Development Finance Office
<b>DSWD</b>	Department of Social Welfare and Development
<b>GFI</b>	Government Financial Institution
<b>INFRACOM</b>	Infrastructure Committee of NEDA
<b>JP</b>	Joint Programme
<b>KALAHI-CIDSS</b>	Kapit Bisig Laban sa Kahirapan - Comprehensive and Integrated Delivery of Social Services
<b>LGU</b>	Local Government Unit
<b>LWUA</b>	Local Water Utilities Administration
<b>MDGF</b>	Millennium Development Goal Fund
<b>NAPC-WASCO</b>	National Anti-Poverty Commission
<b>NAWASA</b>	National Water and Sanitation Association
<b>NEDA</b>	National Economic and Development Authority
<b>NG</b>	National Government
<b>NGAs</b>	National Government Agencies
<b>NGO</b>	Non-governmental Organization
<b>NRW</b>	Non-revenue water
<b>NWRB</b>	National Water Regulatory Board
<b>P3W</b>	President's Priority Program on Water
<b>PAWD</b>	Philippine Association of Water Districts
<b>PFI</b>	Private Financial Institution
<b>PMO</b>	Programme Management Office





<b>PPCP</b>	Public-Private Community Partnership
<b>PPP</b>	Public-Private Partnership
<b>PWRF</b>	Philippine Water Revolving Fund
<b>RWSA</b>	Rural Water Supply Association
<b>SCWR</b>	Sub-committee on Water Resources
<b>SSWP</b>	Small-Scale Water Providers
<b>WATSAN</b>	Water and Sanitation
<b>WHO</b>	World Health Organization
<b>WSP</b>	Water Service Providers



*Pila Balde* Alex Jimenez



## DEFINITION OF TERMS

**Cost-recovery** – refers to recovering or funding the full cost of a project or service including land, building, equipment, staff and operational expenses.

**Financial mechanisms** - a means of providing funds such as bank loans, share capital, reserves or savings, and sales revenue to an entity e.g. WSPs.

**Economic incentives in the water sector** - is a reward or inducement to change behavior as a way of encouraging investments, provided by an institution or organization e.g., state regulators to their partners, investors, clients e.g., WSPs to improve, expand, or upgrade their services to encourage or make viable and attractive service upgrading and expand to unserved or underserved areas. Economic incentives offer flexibility, encourage innovation, cost savings, better management and improve relationships between the private and public sectors.

**Institutional Arrangements** – pertaining to the regulatory bodies tasked with administering the regulatory laws. These bodies may take different forms such as national or local agencies or contract administrators, and all have their own roles, functions, and authority.

**Leveraging** – is a general term for any technique to multiply gains or losses. In the case of WSPs, it can refer to the advantageous condition of having a relatively small amount of cost-yield relative to a high level of returns.

**Output-based aid** – the use of explicit, performance-based subsidies funded by the donor to complement or replace user fees. It involves contracting basic service provision to a third party such as private companies, NGOs, or CBOs with subsidy payment tied to the delivery of specified outputs. The third party can only recover this funding by achieving specific performance outcomes. Generally, OBA schemes finance connection fees<sup>1</sup>.

**Partnerships** - means an agreement between two or more parties (e.g., public-private community) that have agreed to work together in the pursuit of achieving a common purpose e.g., providing water services. This involves cooperation between citizens, communities, business groups, regulators, donors and government entities.

**Regulation** – official rules pertaining to how a particular service is run and financed. Economic regulation, in particular, is needed to (i) balance the interests of the customers and the provider, (ii) ensure that service providers meet their obligation, and (iii) ensure fair pricing<sup>2</sup>.

**Ring fencing** - the practice of a company or institution of creating a legal entity separate from itself in order to protect certain assets. For example, ring fencing may protect assets from taxation, regulation, or allow the company to hide it from creditors<sup>3</sup>.

**Small Piped Water Network** - the delivery of piped water services by a water provider using materials conforming to the main utility's standards that is operated legally to bring affordable, safe, and reliable water to a community until the main utility is able to reach these consumers directly. Once connected to a piped system, beneficiaries pay a





smaller amount for water than what they paid for various non-piped sources<sup>1</sup>.

**Subsidies** – reduction in the market price of a commodity or service. This can include tax allowance or duty rebate for imported materials and equipment, or financial aid (such as a cash grant or soft loan to support a public service, e.g., water provision), to keep prices of tariff low to induce private investment.

**Tariff setting** – any schedule or system of rates, charges, etc. as a tariff on water fees.

**Water Service Providers (WSPs)** - includes formal (regulated) and informal or alternative water service providers, including SSWPs or small scale water providers.

<sup>1</sup> ADB. In the Pipeline: Water for the Poor - Investing in Small Piped Water Networks. 2008

<sup>2</sup> IBID



*Biyaya ng Kalikasan* Joel Forte



*Thirst Quencher* Lister Fil Sandalo



## 1.0 Executive Summary

Output 1.1 of the Joint Programme is about Incentives and Partnership Modalities. It builds on the premise that incentives and partnerships are required to have more accessible, efficient, affordable, and quality water supply to rural areas, particularly waterless areas. Such incentives and partnerships are expected to increase public and private investment in the sector encompassing the whole range of formal and informal water supply service providers.

The study took stock of the existing policies, laws, issuances and rules and regulations that encourage or discourage either public or private entities to invest at the local level; characterized water service providers, produced a compendium of partnerships and incentive modalities that may be applied in waterless and rural areas; produced a framework for implementation of incentive and partnerships on the provision of water services for the poor and a proposed action plan for its implementation.

The study pointed out that while there are enabling policies in place that specifically provide incentives to water service providers such as local water districts, incentives and support for small-scale water providers (SSWPs) are virtually non-existent. Limited financing for water services is a major factor affecting the sector, particularly poor communities where water services are mostly non-existent.

To better provide efficient and effective water services in unserved and underserved areas in the country, the national government can provide a menu of economic incentives such as tax incentives; simplification of customs procedures; additional deduction of labor expense; public financing with governance, performance and regulatory reform objectives; permit and regulatory incentives; use of tradeable permits; recognition and rewards programs; and other incentives that would encourage investments in the country in attaining national economic goals. Incentives can also be subsidies that would jumpstart and render operations in an area financially non-viable despite high costs and low revenues. Subsidies are commonly used tools for inducements even in environmental management. However, subsidies are sometimes criticized because government helps bear the costs that should otherwise be the responsibility of the investor or service provider.

Government should also support partnerships for universal service coverage through policies that reframe the mission of regulators and of water policy bodies that emphasize providing adequate water to people in unserved areas. It should support, strengthen incentive mechanisms and partnership modalities to induce personnel, regulators, service providers and politicians to act collectively and help achieve universal coverage. Governments and donor agencies should emphasize that access to financial resources goes hand in hand with good governance by creating an environment favorable to private investment, by reducing investment risks, and by providing credit support through grants, loans and/or guarantees. In addition, rationalization of financing has to happen to ensure efficient and effective allocation of scarce resources.

The proposed framework for the implementation of Incentives and Partnerships on the provision of water services for the poor and the proposed action plans and recommendations merit serious consideration if the commitment towards achieving universal coverage is to be met soon.





## 2.0 Introduction

The UN-Spanish Government Joint Programme, MDG-F 1919, “Enhancing Access to and Provision of Water Services with the Active Participation of the Poor,” is envisioned to fill in the “soft” component gaps in current programs of the national government that focus only on infrastructure provision. The Joint Programme is expected to contribute to the provision of more accessible, efficient, affordable, and quality water supply to rural areas, particularly waterless areas, through the provision of complementary support to the current efforts of the Government under the President’s Priority Program on Water (P3W). Output 1.1 of the Joint Programme will produce a compendium of possible incentives and partnership modalities that have been proven effective by international and local experiences which have been reviewed and assessed for possible application in waterless communities in rural areas in the Philippines. Such incentives and partnerships are expected to increase public and private investment in the sector encompassing the whole range of formal and informal water supply service providers.

Expected deliverables for Output 1.1 include the following:

- a) Taking stock of existing policies, laws, issuances and rules and regulations that encourage or discourage either public or private entities to invest at the local level;
- b) Characterization of WSPs in terms of operation and business practices;
- c) Compendium of partnerships and incentive modalities;
- d) Assessment of locally and internationally available partnership and incentive mechanisms for possible application in waterless and rural areas while considering the water service providers (WSPs) existing in waterless/rural areas;
- e) Framework for partnerships and incentives prerequisite in the provision of water supply services in poor and waterless communities; and the
- f) Action plan for the implementation of the recommended and innovative incentive/ partnership mechanisms by different WSPs, including alternative providers.

The Study Team used several participatory approaches such as key informant interviews, focused group discussions and individual consultations in generating and validating information from various stakeholders in the water sector. Desk reviews of policies, programs, incentives and partnerships and related literature locally and internationally on water supply provision were also undertaken.

The various types of water service providers in the country can be characterized according to management models, operations and business practices. Large service providers are mostly private corporations or water districts while SSWPs include rural water service associations (RWSAs), barangay water service associations (BWSAs,) water cooperatives, homeowners associations or small individual private businesses. Most SSWPs are unregulated and operate outside of the formal set-up.





### 3.0 Incentives and Partnerships on the Provision of Water for the Poor

Economic incentives in the water sector are designed to ensure a mutually beneficial behavior among parties to encourage water service providers to increase investments to improve, expand, or upgrade their services especially in unserved or underserved areas in the country.

There are policies in place that specifically provide incentives to water service providers such as local water districts. However, incentives for SSWPs are virtually non-existent. Limited financing for water services is a major factor affecting the sector, particularly poor communities where water services are mostly non-existent.

To better provide efficient and effective water services in unserved and underserved areas in the country, the national government can provide a menu of economic incentives such as tax incentives; simplification of customs procedures; additional deduction of labor expense; public financing with governance, performance and regulatory reform objectives; permit and regulatory incentives; use of tradeable permits; recognition and rewards programs; and other incentives that would encourage investments in the country in attaining national economic goals.

Incentives can also be subsidies that would jumpstart and render operations in an area financially viable despite high costs and low revenues. Subsidies are commonly used tools for inducements even in environmental management. However, subsidies are sometimes criticized because government helps bear the costs that should otherwise be the responsibility of the investor or service provider.

Table 1 and 2 is a summary matrix of recommendations on Incentives and Partnership Modalities.



*Bitak* Joel Forte





**Table 1. Matrix of Recommendations on Incentives**

Incentives			Administrator	Target Group/s	Assessment/Remarks/Constraints/Issues
Type	Specific Mechanism	Description			
Return on Investment	Regulation	Tariff setting parameters allow the WSP to recover all costs and even earn a reasonable level of income	Economic Regulator	WSPs	Study and consider exempting investments in water provision in risky areas from the existing rate limitation of 12% on return on investments
Subsidy	Output-based provincial subsidies	In the short-term, output-based provincial subsidies for RWSAs and cooperatives can be funded out of special levies. The Local Government Code allows LGUs to recover some of the costs for infrastructure projects that specifically benefit establishments and properties at the urban center.	LGUs	RWSAs and cooperatives	Templates and model ordinances that would make implementation straightforward have to be developed.
<b>Incentive Mechanisms that Need Strengthening</b>					
Financial support	National matching grant to LGUs	Stronger incentives for LGU investments even where a water district exists	National government	WSPs	Water district and LGU responsibilities in providing water to non-viable areas need to be clarified.
Financial support	National grants to LGUs	Stronger incentives for LGUs to encourage community counterpart finance or capital build-up, even in poor waterless communities	National government and regulators	LGUs	Policy on tariffs should support internal cash generation and tariff-adjustment exercises should be seen as resource mobilization exercises for financing investments in waterless barangays. The buy-in of HH into community-level service provision is often a necessary input for the resilience and future expansion of service provision.
Regulation	Performance bonuses, eg for NRW reduction	Performance incentives that will encourage water utility staff members to become more efficient in bringing quality services farther afield.	Regulator	WSPs	In some water districts, performance bonuses for WD staff have been introduced to hasten the replication of good management techniques that promote efficiency – similar to what was done by Metro Manila Concessionaires
Micro loans to poor consumers	A seed capital for establishing a revolving fund for microfinance	Incentives to induce innovations for microfinance for water service connections to poor waterless communities.	National government	WSPs	Can be supported by an output-based aid arrangement or can be piloted in P3W areas with certain modifications.



**Table 2. Matrix of Recommendations on Partnership Modalities**

Partnership	Objective	Description	Case	Remarks
National-local or investor-community partnership	Provide conduits for performance-based fund flows to WSPs.	Conduit for public funds for waterless communities might plausibly be central concessionaires, cooperative federations, and professional organizations of water district managers or local government units.		Banks and investors do not know how to assess business proposals in water provision, a transitory stage might be needed where they could work with conduits of funds
Poblacion-periphery partnerships between large utilities and SSWPs	Expand coverage to poor waterless areas	Large private concessionaires, large LGU-owned utilities and water districts that have economies of scale can be compelled through regulatory mandates to deliver cross subsidies for primary and secondary lines that supply to SSWPs in poor communities or rural water systems that are out of their present reach but are within their designated service areas.	Metro Manila experience	On the strength of their access to long-term credit, these large utilities can be compelled by regulators to support SSWPs in the peripheries through their capital expenditure (CAPEX) budget and loan agreements.
<b>Partnership Modalities that Need Strengthening</b>				
NWRB-SSWP partnership	Increase the credibility and credit worthiness of SSWPs	Partnering with NWRB to help reduce the political risks faced by SSWPs.	The case in Zambia and Ho Chi Minh City shows that once formalized, alternative providers are better able to invest in service expansion and access more financing.	Light-handed regulation is being developed under the MDG-F 1919 program.
WD-LGUs-Local Development Academy-Academe	To improve and achieve greater performance of WSPs	Partnerships for capacity development of SSWPs		The DILG program of establishing and strengthening WATSAN Councils around the country can coordinate and provide direction to the capacity development of BWSAs and RWSAs in various municipalities and cities.



WD-LGU-SSWP	Areas far from the pipes of the water district are supplied by a private provider or SSWP with water of the same price and quality as that enjoyed by poblacion dwellers	Partnerships between water districts and SSWPs of waterless barangays facilitated by LGUs and included within the planning grid of LGUs	Similar to what is being done in Brgy Telabastagan in San Fernando, Pampanga	LGUs can map the partnership relationships and the specification of a division of labor between big and small water providers; clear time frames and regulatory arrangements (inscribed in WD-LGU-SSWP contracts) can mitigate the proliferation of conflicts of jurisdiction and endless legal disputes between complementary service providers.
Inter utility partnerships	Compare performance to achieve commercial viability	Partnerships that would enable water utilities, whether public or private to compare efficiencies and techniques appear to be critical so that large water utilities can help each other transform their scale into commercial viability and viability into financing for expansion into previously unserved areas.	Utility benchmarking	Utility benchmarking may become even more helpful if particular kinds of cost items are benchmarked (e.g., water source development, water treatment, transmission, storage and distribution, billing, collection and NRW reduction).
LGU-DPWH-NGO partnerships in rainwater harvesting for household use	Provide water to the poor and disadvantaged	Rainwater harvesting is a low-cost technology that can provide water to the poor and disadvantaged while at the same time conserve ground and surface water resources. It also provides safe water during calamities and extreme weather conditions.	Kahublagan sa Panimalay Foundation and the province of Capiz	Can be included in the P3W list of priorities



## 4.0 Partnerships in the Provision of Water for the Poor

Public-Private Community Partnerships (PPCPs) is a promising model in terms of sustainability and active stakeholder participation. It ensures implementation of a strategic framework for making participation a more viable service delivery option for government. Local institutions formed with greater emphasis on participation have survived longer than those that have focused only on the physical component as it inculcates “a sense of ownership.” Time and resources for social preparation and capacity building of stakeholders have to be included in the feasibility study of a water supply project. Closer attention should be given in crafting an enabling institutional environment in which key roles and responsibilities are clearly defined and allocated among all key stakeholders to ensure significant improvement and sustainability of the service delivery while at the same time encouraging private participation.

**To foster good governance, LGUs and NGAs must lead by example. They can and should facilitate transparency by:**

1. Ensuring accountable and transparent records and the free flow of information;
2. Compliance with government’s financial and procurement laws and procedures;
3. Being informed about current and reasonable prices of project inputs obtained through fair and thorough canvassing; when and where possible, involving the community in the canvassing and procuring of materials;
4. Ensuring community participation and the community’s ability to understand the project and discern values;
5. Timely and thorough monitoring (especially on financial and procurement matters), maintaining check-and-balance systems;
6. Adopting transformational political leadership, that is, emphasizing on meeting the general community’s interests over individual needs;
7. Transparent and conscientious resource and project management that reduce project costs and increase sustainability.



*Bigat at Pawis sa Tubig ng Buhay* Jason Cardente



*Masayahing Nag-iigib* Jason Cardente



## 5.0 Constraints to the Provision of Water for the Poor

Problems of management, financial and technical capacity hinder the sustainability of BWSAs, RWSAs and cooperatives. Tariffs are set too low to cover the cost of maintenance or replacement of core resources. Operational and technical capacity is limited in order to draw up a cohesive plan of action and monitor operations and address conflicts that arise. There is no institution that can provide them the assistance similar to the Local Water Utilities Administration's (LWUA) role in helping the water districts. SSWPs need assistance to overcome the many constraints they face in establishing, operating, sustaining and expanding their water provision activities, especially to poor areas and households.

### Constraints Faced by SSWPs

- **Financial Constraint** (Cash flow problem, bank financing, equity and subsidy issues)
- **Regulatory Risks and Legal Constraints** (politicized tariff-setting, aggressive central utilities, free entry problem, lack of capacity of the regulator)
- **Organizational and Capacity Constraints** (absence of qualified staff, limited know-how on O&M, business planning)
- **Physical Constraints** (distant source, quality of water supply, lack of water source, etc.)



## 6.0 Study Recommendations

Government should support partnerships for universal service coverage through policies that reframe the mission of regulators and of water policy bodies that emphasize providing adequate water to people in unserved areas. Even in the presence of the appropriate policies and partnerships, incentive mechanisms will be needed to induce personnel, regulators, service providers and politicians to act collectively and help achieve universal coverage. Governments and donor agencies should emphasize that access to financial resources goes hand in hand with good governance by creating an environment favorable to private investment, by reducing investment risks, and by providing credit support through grants, loans and/or guarantees. In addition, rationalization of financing has to happen to ensure efficient and effective allocation of scarce resources.

### 6.1. New Incentive Mechanisms and Partnership Modalities

The ‘new’ incentive mechanisms and partnership modalities are ‘new’ only in the sense that they have not yet been established in the country. Public-private-community partnerships are common locally and internationally but a Public-Private-Partnership with LGUs at the center is a new arrangement for the Philippines.

- a. **Incentives for entrepreneurs making risky investments in unserved areas.** An investment may be deemed risky if it is in a rural or peri-urban jurisdiction that is not part of the short- to medium-term expansion plan of a central utility. The legal requirement that limits returns on investments (financed by loans and equity) to 12% is a disincentive to entrepreneurs and their financiers. An incentive mechanism that can address this is to declare that pre-operational returns of investors—defined as those returns during the period before acquiring a Certificate of Public Convenience (CPC)—will not be subject to the 12% limitation because of the high financial risks of lending to a coop or SSWP that is just discovering the viability of its enterprise.
- b. **Financial incentives for grassroots associative water systems expanding in unserved and/or in commercially unviable areas.** In the short-term, output-based provincial subsidies for rural water associations and cooperatives can be funded out of special levies. An LGU is allowed by the Local Government Code to recover up to 40% of the costs of projects that directly increase property values due to improved flood control, increased access, etc. What is needed is the development of templates and model ordinances that would make implementation straightforward.
- c. **National-local or investor-community conduits for performance-based fund flows.** Because banks and investors do not know how to assess business proposals in water provision, a transitory stage might be needed where they could work with conduits of funds (e.g., water districts, water service provider federations, etc.) directed at SSWPs.
- d. **Regulator-induced poblacion-periphery partnerships.** Large private concessionaires, large LGU-owned utilities and water districts that have economies of scale can be compelled through regulatory mandates to accelerate universal service coverage. Such central utilities can enter into partnerships that deliver cross subsidies for primary and secondary lines that supply to small scale water service providers in poor communities or to rural water systems that are out of their present reach but are within their designated service areas.



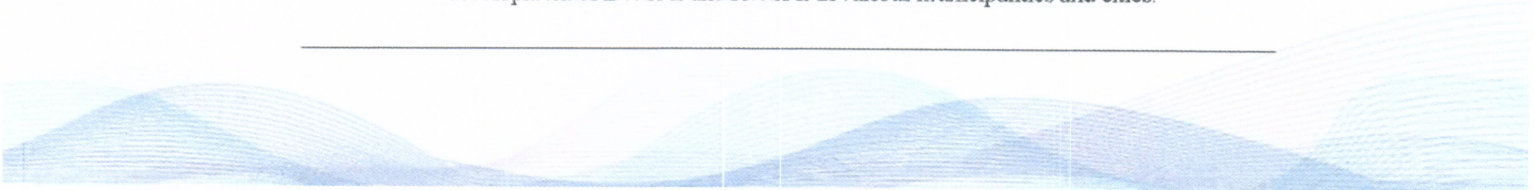


## 6.2 Strengthening of Existing Incentive Mechanisms and Partnership Modalities

- a. **Stronger Incentives for LGU investments even where a water district exists.** The financial support of LGUs remains essential in the overwhelming majority of water district jurisdictions. Stronger incentives must be given to LGUs to partner and coordinate with water districts so that they continue to perform water service functions devolved to them.
- b. **Stronger incentives for LGUs to encourage community counterpart finance or capital build-up, even in poor waterless communities.** The national government can provide matching grants for LGUs that are able to induce communities to contribute resources for the achievement of universal service coverage. Households and communities have always mobilized resources to provide for essential services.
- c. **Performance incentives that will encourage water utility staff members to achieve requisite efficiencies that will bring quality services farther afield.** Within large water districts, performance bonuses for water districts staff have sometimes been introduced to hasten the replication of good management techniques that promote efficiency. These incentives are similar to the incentives for the achievement of NRW (non-revenue water) reduction target in Metro Manila concessions.
- d. **Incentives to induce innovations for micro-finance for water service connections.** Providing support for the establishment of microfinance for water connections for the poorest can serve as an incentive to SSWPs as well as central utilities to establish or extend water systems into poor waterless communities. This can come in the form of a seed capital for establishing a revolving fund for water service micro-finance that can be supported by an output based aid program similar to what was done in the East Zone of Metro Manila. This time around, output-based aid can be coursed through LGUs or water districts in rural areas; as in the East Zone concession payments, which can be reimbursed after the outputs have been accomplished.

## 6.3 Existing Partnership Modalities That Need Strengthening

- a. **Partnering with NWRB to help reduce the political risks faced by small scale water service providers.** Legitimizing small water service providers through the registration and permit-granting processes of the NWRB through light-handed regulation can facilitate the flow of funds to SSWPs and increase the credibility of SSWPs.
- b. **Partnerships for capacity development of SSWPs need to be developed in order to improve and achieve greater performance.** If the DILG for instance is made ultimately accountable for the achievement of universal service coverage through LGUs, it should be empowered to require specific water districts to set aside financial resources and personnel who would fulfill partnership obligations with LGUs. LGUs can broker the provision of capacity development to SSWPs in its jurisdiction with academic institutions, Local Development Academy branches or water district federations. The DILG program of establishing and strengthening Water and Sanitation (WAISAN) Councils around the country can coordinate and provide direction to the capacity development of BWSAs and RWSAs in various municipalities and cities.





- c. **Partnership between water districts and smaller service providers of waterless barangays facilitated by LGUs.** Municipal and barangay LGUs can facilitate partnerships between water districts and small water providers so that areas far from the pipes of the water district are supplied by a private provider with water of the same price and quality as that enjoyed by poblacion dwellers. LGUs can map the partnership relationships and the specification of a division of labor between big and small water providers and help mitigate the proliferation of conflicts of jurisdiction and endless legal disputes between complementary service providers.
- d. **Twinning and benchmarking exercises** should be strengthened and expanded to learn from the industry's best practices and innovators. Partnerships that would enable water utilities, whether public or private to compare efficiencies and techniques appear to be critical so that large water utilities can help each other transform their scale into commercial viability and viability into financing for expansion into previously unserved areas.
- e. **LGU-DPWH-NGO partnerships in rainwater harvesting for household use** need to be promoted in difficult and hard-to-reach areas, island barangays and flood prone areas as climate change adaptation measures. The Department of Public Works and Highways (DPWH) is already planning to harness rainwater for agricultural use in flood prone areas; rain water collection for household use can also be included. The setting up of rainwater collection systems for household use can also be included in the P3W list of priorities.



*Moving on for Life James Ramirez*



## 7.0 Framework for the Implementation of Incentive and Partnerships on the Provision of Water Services for the Poor

This framework describes the partnerships, incentives and accountabilities that are crucial in bridging the gap between the supply and the demand for funds to achieve universal coverage for water. There are important elements that are still being assembled on the supply side such as credit facilitation instruments for water districts at LWUA, performance-based grants scheme from Municipal Development Fund Office (MDFO) and from output-based aid sponsors and microfinance schemes for water connections.

As shown in Figure 1, incentives to water utilities are provided by national government agencies, local government units, public and private banks and bilateral and multilateral agencies and institutions. However, there is a range of constraints faced by different service providers in their attempt to achieve viability in underserved areas. This analytical framework proposes an approach to unpacking the challenges faced by water utilities such as: those confronted by large utilities that may expand into waterless areas; those capabilities that small utilities must develop to set up the internal metrics for ensuring accountability to its owners and stakeholders and to establish credibility when attracting outside finance; readiness of a small utility when it achieves some measure of bankability to address the risks posed by central utilities that could extinguish the value of its hard-earned capital, and last, those of small LGU-owned utilities and water districts that require outside support to sustain the path towards universal coverage for their service area.

The need for an effective economic regulator underscores the expected behavior of large water service providers and private utilities in delivering improved levels of service and expanded service coverage to underserved or unserved areas.

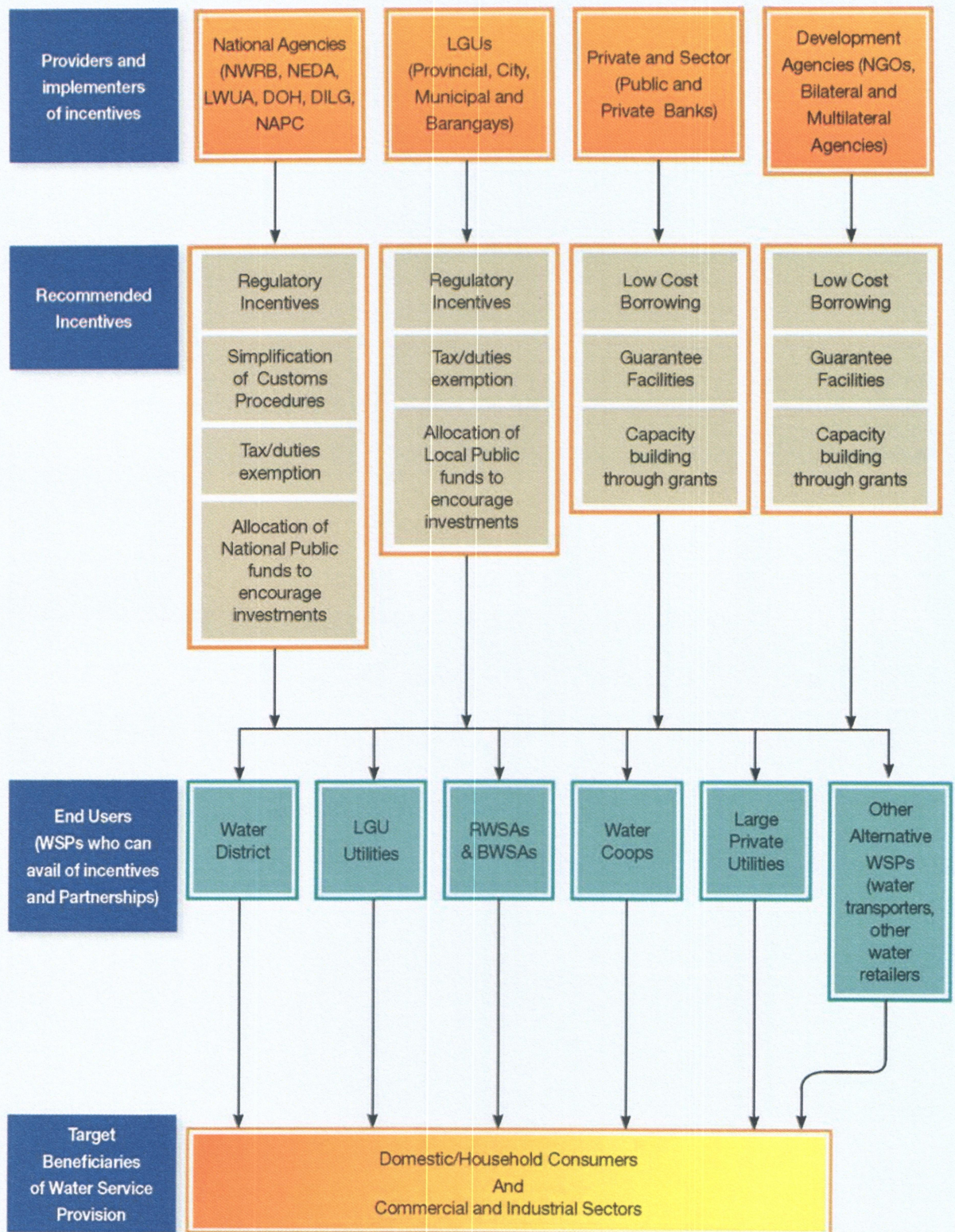
Incentives and technical assistance need to be given to LGUs to raise more revenues and improve performance. This will entail benchmarking LGU financial and institutional performance, and introducing performance-based criteria to the national government's fiscal transfer programs to LGUs to incentivize revenue mobilization and performance enhancements. Technical assistance to LGUs in revenue mobilization and infrastructure investment planning and preparation is important.

The national government should strengthen ongoing efforts in advancing local inter-jurisdictional cooperation by providing more authority to the regional development councils and giving higher priority to the province level, with regard to intergovernmental fiscal transfers. The central government can also help in developing multi-district or multi-province surface water development, which cannot be done within the means available to municipal or city governments. It is certainly very important for local governments to be made more accountable for achieving universal service coverage and there are grants for water provision that were and are still given to local governments that will not require them to dip too much in their own resources.





**Figure 1. Framework for the Implementation of Incentive and Partnerships on the Provision of Water Services for the Poor**





This implementation framework shows that water provision, including provision of incentives as shown in Figure 1 involves multiple agents and/or players. There are a number of recommended incentives that they may help facilitate to many different ways to expand provision of water services to the poor.

### **A. Incentives and Partnership Modalities with NGAs**

National government agencies play important roles in encouraging large and small water providers to expand to waterless and underserved areas through various forms of incentives and partnership modalities. National government agencies involved in the water sector such as NWRB, LWUA, DOH, DILG and NAPC can provide regulatory incentives, simplification of customs procedures, tax/duties exemptions and national public funds allocation to encourage investments in waterless and underserved areas. At the national level, it will be important to synchronize and rationalize rules and priorities for cost sharing mechanisms. The study proposes to look into the following:

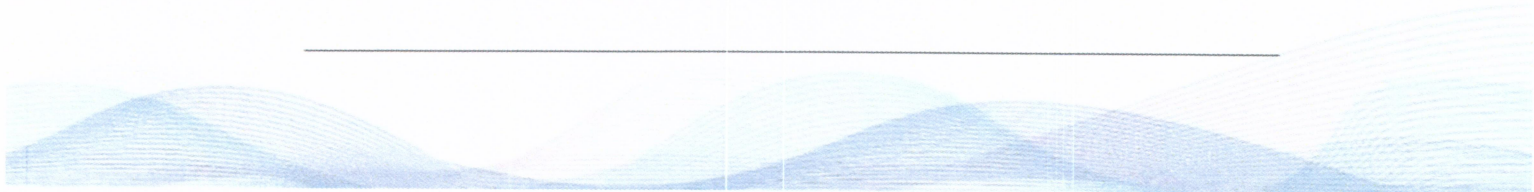
1. Performance based incentives, external and internal benchmarking and twinning arrangements
2. Incentive based regulation
3. Demand side financing and partnerships to bridge the gap between supply and demand
4. Risk Management to foster partnership with other water utilities
5. Strengthening existing national-local cost sharing

### **B. Incentives and Partnership Modalities with LGUs**

Provincial and municipal governments are in a position to facilitate the provision of water in their respective areas of jurisdiction. If the central utility does not have sufficient scale and financial muscle to subsidize peri-urban and rural water systems, it is possible to get these funds using the revenue base of the local government. The provincial LGUs may use its own funds to create a vehicle for output-based provincial subsidies for RWSAs, for instance.

### **C. Incentives and Partnership Modalities with Public and Private Banks, Bilateral and Multilateral Institutions and Non-Government Organizations**

Public and private banks can provide access to investment funds for water supply service delivery programs of SSWPs. Various innovative arrangements can be developed to facilitate micro-credit facilities for SSWPs. On the other hand, development partners can support the creation of guarantee facilities, output based aid and capacity building investments.





## 8.0 Action Plans

The action plan focuses on strengthening partnerships and mechanisms to put in place incentives and financing schemes to ensure universal coverage for water. It identifies four key objectives and corresponding approaches and operational requirements culled from the framework on partnerships, incentives and accountabilities that are crucial in bridging the gap between the supply and the demand for funds to achieve universal coverage for water. The key objectives of the action plan are:

- Define who will be accountable for ensuring universal coverage for water provision
- Mobilize local resources to encourage provision of water in poor, waterless areas and municipalities
- Strengthen partnerships between SSWPs, WDs and government to encourage universal coverage on water provision.
- Strengthen Public-Private-Community Partnerships in water provision for poor communities
- Enhance the viability and commercial orientation of SSWPs and non-functional water districts
- Adopt climate change adaptation measures in water provision for poor communities

The Study Team proposes that **LGUs be the primary institutions accountable for ensuring universal coverage for water provision in their respective areas.** As such, LGUs need to develop long-, medium- and short-term development and investment plans on water provision, establish partnerships with water service providers and other stakeholders and be willing to craft enabling policies and provide start-up and/or counterpart financing to provide water to unserved areas and poor constituents.



*Cooling Off* Joaquin F. Go, Jr.





## 9.0 Policy Recommendations

### Strengthening Institutional Accountability

1. The Department of Budget and Management (DBM) in cooperation with the Department of Finance (DOF) and the DILG should move forward with Joint Memorandum Circulars that could begin the process of defining the major final outputs (MFOs) of LGUs and sub-units. Having MFOs will establish the accountability of those in the local Executive Department to their local Sanggunian. These new information templates for enhancing local planning and inter-agency accountability can become part of the Local Government Performance Monitoring System (LGPMS) of the DILG.
2. Amend the NEDA InfraComm (Infrastructure Committee) Resolution on the delineation of responsibilities between LGUs and water districts where the present InfraComm says that water districts financed by LWUA should only implement financially viable projects, thus delineating the role and responsibility of LGUs in supporting projects for non-viable areas. This InfraComm Resolution was proposed as an amendment to NEDA Resolution Number 5 series of 1998. The review should try to achieve a four-fold objective:
  - a. **Strengthen the LGU-water district delineation of responsibilities to further affirm LGU institutional accountabilities for service delivery.** It is recommended that LGUs be made accountable for the non-implementation of their medium-term plans for the progressive realization of service level improvements in financially non-viable areas. Medium-term plans have to be articulated in annual investment programs.
  - b. **Coordination and partnerships between LGUs and water districts.** It is also proposed that the LGU and the water district identify those areas that are “almost financially viable” and for which LGU action may be needed to push those areas across the threshold of viability. This will probably require an unbundling of water service investments towards service level improvements into its various



*Dying Water* Ernie Peñaredondo



sub-components in order to specify the limits of what the water district is able to finance, and which aspects the LGU and also the beneficiary community may have to take on.

A manual of operations and a template of ordinances and executive orders on LGU-water district cooperation should be produced that can be customized for other areas nationwide. This can be patterned from the successful Zamboanga City - water district cooperation in bringing water to waterless areas.

- c. **Policy on tariffs should support internal cash generation and tariff-adjustment** exercises should be seen as resource mobilization exercises for financing investments in waterless barangays. It should be a matter of policy for the water district and local government tariff regulators to adjust tariffs to maximize internal cash generation, subject to affordability thresholds for the poor and near-poor households. The water district and the LGU should both have a ranked list of medium-term investments, including those that can come into consideration if more financing becomes available.
  - d. **Accountability relationships need to be built, as far as water district technical support for non-viable areas is concerned.** The LGU should have an inventory of technical and organizational capacity support that community-level water service providers must require; such support should include support for participatory decision-making in the course of developing feasibility studies and work and financial plans.
3. The DILG should instruct local governments to pursue their mandate of supporting water provision in waterless areas by brokering formal commitments between RWSAs and BWSAs on the one hand, and the nearest water district, NGO or university/PAWD (Philippine Association of Water District) office that can provide assistance in: i) organizational strengthening, ii) asset turn-over procedures to central utilities, iii) tariff-setting and CPC compliance, iv) technical capacity building for NRW reduction, iv) feasibility study development, etc.

Where the supporting entity is unable to provide free services, it will be the duty of the local government to provide contract-based compensation for these entities so that the waterless communities may tap their expertise. In the case of water districts, tariff adjustments should include a component that will directly support outreach to waterless communities. The NWRB can also request the water districts to review their tariffs and amend these if there is no earmarked amount for providing technical support for RWSAs and waterless communities that would like to set up RWSAs or BWSAs.

#### **Clarifying/Strengthening Regulation**

4. Re-calibrate the mission statement of regulators so that their aim will be to take a pro-active role in generating financing for universal coverage. This can be done by ensuring that jurisdictions with significant scale economies will finance expansion plans and operate facilities in less well-endowed jurisdictions. Tariffs in central urban areas should be adjusted upwards, while ensuring that the poor households in the National Housing Targeting System (NHITS) are levied lower charges or are given direct consumption subsidies similar to Chile's approach. SSWPs should be encouraged to bid to operate sub-systems if they can offer lower costs. To facilitate this





process, the DILG, LGUs, LWUA and NWRB can do the following:

- i) identify areas that have significant economies of scale as evidenced by their low operating costs;
- ii) support the development of associated tariff adjustment plans to revise CPCs and water district plans;
- iii) propose the development of a Chile approach of instituting water connection and direct consumption subsidies for the poorest households in order to mitigate the effects of higher tariffs where such a grant component can be funded out of output-based aid (OBA) grant proceeds from returns accruing from the pooled second-generation funds of the MDFO and from additional annual budget appropriations; and
- iv) with knowledge of the investment plans, demographics of the customer base and initial tariff structures in the locality, the NWRB can provide support for pre-approved default tariff adjustment plans with their associated investment plans, as well as the consumer subsidy plans from the central government.

#### Performance-based Financing

5. InfraComm should propose a NEDA Board Resolution that output-based aid programs and resources should prioritize the waterless municipalities in NAPC's P3W list. The resources to be devoted to poorer jurisdictions outside of the highly-urbanized cities will come with stronger performance-based dimensions as well as local resource mobilization conditionalities.



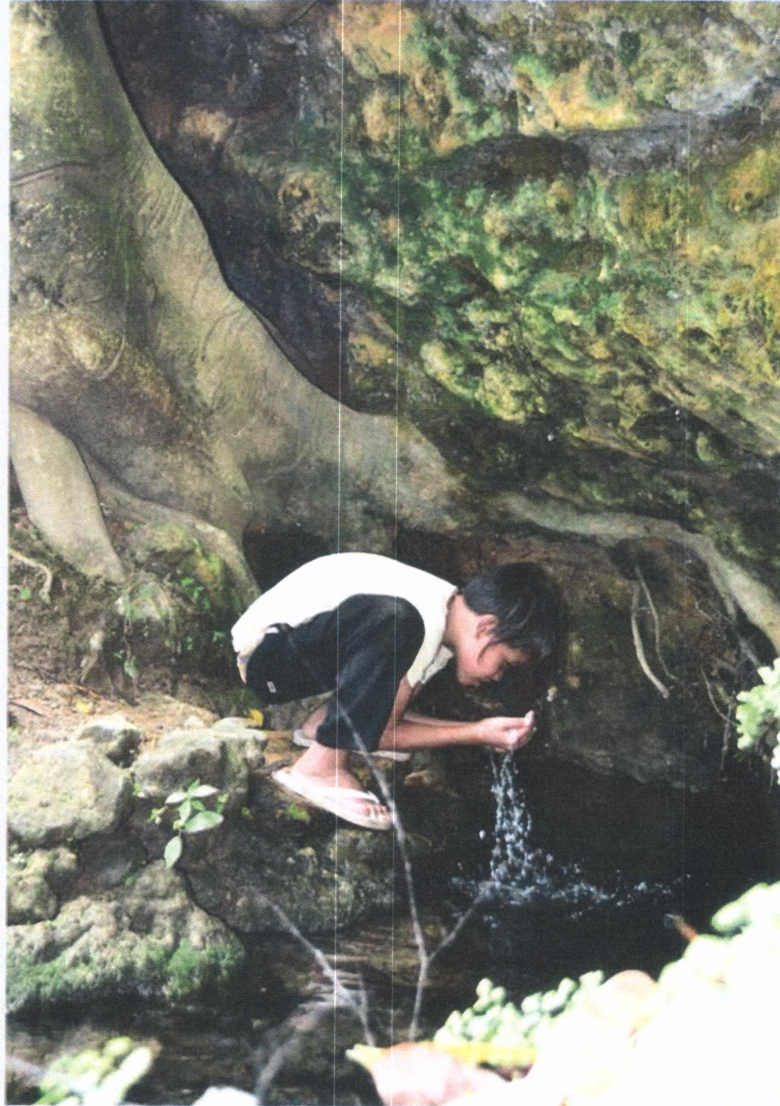
*Bottoms Up* Ernie Peñaredondo



*The Innocent* Jason Cardente



6. Possible NEDA InfraComm Recommendations to the DOH and the NAPC for P3W Guidelines and national government-local government unit (NG-LGU) cost-sharing rules of the NEDA Board. Grants for local governments that exceed those allowed under the NG-LGU cost-sharing rules should be based on stricter rules that introduce performance-based evaluation and local resource mobilization conditionalities to encourage local financing of service expansion plans and to increase the achievement of investment outcomes.
7. NG-LGU cost-sharing rules and subsidies should be articulated for barangays and their PPP partners. Most waterless contexts are barangay-level realities. The access of community-level service providers to grants following NG-LGU rules, including MDFO grants and other grants, may be encouraged where these directly address millennium development goal (MDG) targets such as waterless areas. Provincial or municipal clearinghouses may be established to reduce transaction costs and to ensure compliance with procurements and performance protocols. The province or municipality may also be encouraged to contribute some of the counterpart grants that may be administered by the MDFO.



*Spring of Thirst* Art Fill Sandalo



## NOTES ON THE STUDY

- a. The full study was submitted in December 2011 by a Study Team composed of Ms. Minerva G. Gonzales (Team Leader), Mr. Enrique N. Nunez, Mr. Edwin R. Celestino and Mr. Jude Esguerra.

**Minerva G. Gonzales (Team Leader)** is a natural resource management specialist with extensive experience in the promotion and protection of economic, social and cultural rights, including the right to water.

She has more than 30 years of experience in community-based management of natural resources including policy formulation and review, sustainable development work, general NGO management, community organizing, advocacy and networking with government agencies, local government units and donor agencies, project preparation, development, implementation, monitoring and evaluation.

She has engaged with various sectors on water policies and the implication of climate change to water availability to poor and vulnerable sectors. She has been engaged as consultant by several national government agencies and multilateral donor agencies.

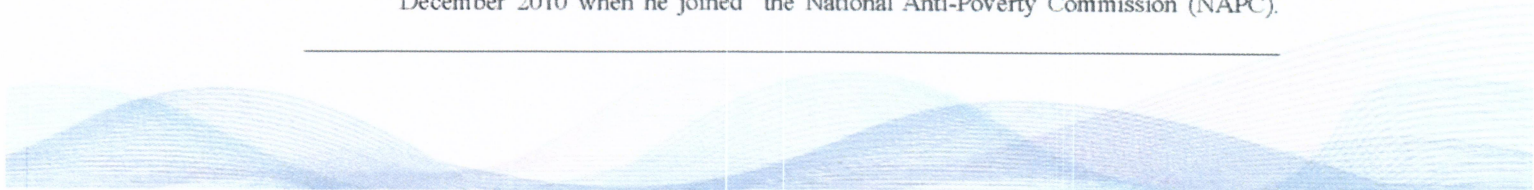
**Enrique N. Nunez** is an economic/financial specialist as well as a natural resource management specialist with more than 20 years of experience in protected areas management, watershed management, conservation financing, payments for ecosystems services, local policy development on water and watershed protection, project and program evaluations, and other work related to economic and social development, particularly in the rural areas.

He has a background in environmental economics and development policy having taken up additional courses with the World Bank Institute and the Environment and Economic Program for South East Asia funded by the International Development Research Centre. He also has a background in knowledge management and business intelligence.

He has demonstrated several experiences in project management, policy formulation and review, implementation, project evaluation, having held management positions for NGOs and consultancy work for international and multilateral agencies.

**Edwin R. Celestino** is an institutional development specialist and holds a Ph.D. in Community Development and Agribusiness Management. He introduced the community-managed water supply system as an innovative strategy to enlist people's active participation in water projects funded through bilateral and multilateral programs. He planned, designed and implemented knowledge building activities to enhance the institutional, organizational and human resources capacity of the water associations in their operation and maintenance. He was team leader of a Focal Rice Policy Group under a provincial government. He has developed plans and programs for a state university and was engaged in promoting a regional coconut diversification program through the FFS, an alternative education system managed and operated by an NGO. He was also a consultant to a number of donor-funded projects in the Philippines and abroad.

**Jude Esguerra** was executive Director of the Institute for Popular Democracy until December 2010 when he joined the National Anti-Poverty Commission (NAPC).





He has a Master's Degree from the UP School of Economics and an undergraduate Degree in Sociology from the UP - Diliman. In terms of the water sector, he has been involved in action-research on matters concerning universal service coverage in the Metro Manila water concessions and the rationalization of national government water subsidies for local governments. He is an advocate for reducing the risks faced by community-led water service providers.

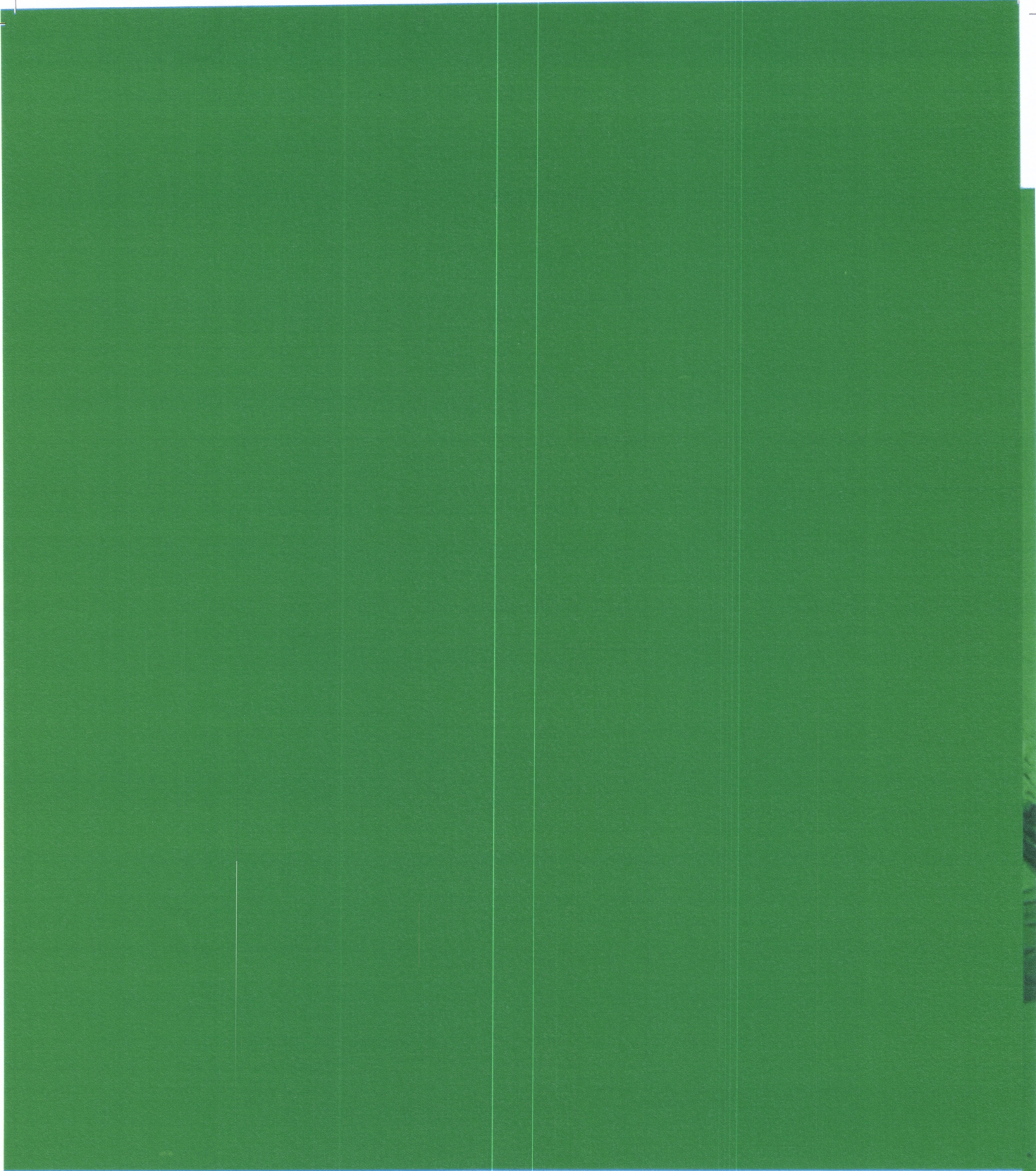
- b. A copy of the full study report can be requested from the National Economic and Development Authority. Interested parties may contact Ms. Kathleen P. Mangune, Project Manager (kpmangune@neda.gov.ph).
- c. This summary document was prepared by **Rosario Aurora L. Villaluna** based on the final report of the Study Team. This report feeds into the Integrated Policy Document on Pro-poor Water Supply.

Ms. Rosario Aurora L. Villaluna is currently the Chairperson-elect of the Philippine Water Partnership and is a member of the NEDA Sub-Committee on Water Resources. She is currently the Chairperson of the Philippine Ecological Sanitation Network and the Executive Secretary of the Streams of Knowledge.



*Everyday Life by the River* Eric Merced





Implementing Partners:



Department of the Interior  
and Local Government



National Water  
Resources Board



National Economic and  
Development Authority



United Nations Chil-  
dren's Fund



United Nations Development  
Programme

