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Coping with COVID-19: Financing Opportunities for LGU Recovery

Before the spread of the COVID-19 pandemic this year, Mayor Arthur Despi of Bantayan in Cebu was working to improve conditions in his municipality. For one, their local government unit (LGU) wanted to improve the municipal water system, including the building of desalination plants. Worth about P225 million, the project had received the go-signal of the Department of Public Works and Highways, and the LGU was considering a loan to finance part of the project

However, when COVID-19 began affecting their residents' food security and livelihoods, the Bantayan LGU had to devote a good portion of the funds — about P45 million — to cope with more immediate needs of the most affected sectors including drivers of *traysikad*, tricycle, *habal-habal*, jeepney, and minibus. Another P24 million went to food — 5 kilos of rice each for some 1,200 families.

Sourcing funds is now more challenging, as local officials like Mayor Despi must address not just COVID-19 realities

but also other development concerns. While LGUs can tap resources that are available from government lending institutions, only a small portion are accessing these resources.

To address this gap, Rare Philippines organized a webinar last June 23, 2020 in partnership with the Bureau of Local Government Finance (BLGF), an agency of the Department of Finance, so that LGUs could learn more about financing opportunities from government lending institutions. Officers from the Development Bank of the Philippines (DBP) and the Land Bank of the Philippines (LBP) gave inputs and answered questions from 70 local chief executives and LGU personnel.

"Amid the pandemic, LGUs need to mobilize their resources and tap alternative resources for response and recovery efforts," said Dr. Jose Arnold M. Tan, Deputy Director III of the BLGF, in his opening remarks. This is the LGUs' mission because in times of calamity, LGUs are considered "frontline forces of the government" to ensure the people's well-being, he said.



Barriers to Borrowing

The knowledge gap on financing opportunities was evident in a pre-event survey which showed that majority of the LGU participants (57.69%) are not aware of financing opportunities available to LGUs. At the same time, an overwhelming portion (92%) is interested in availing of financing products for their priority projects.

Many LGUs cited the lengthy application process as well as limited capability to fulfill technical requirements, such as a project feasibility study, as barriers to seeking loans. Benito "Jun" Secuya, Jr., a member of the Local Finance Committee of the municipality of Badian, Cebu, still remembers the "long and tedious" procedures that their local government had to go through to secure credit financing under a World Bank program sometime in 1988. "Madugo" is how Secuya describes the process, which took three years from project conceptualization to the release of the first tranche. The Badian LGU had to approach several national agencies for the technical expertise required to avail of the grant.

Other LGUs echoed Badian's experience in the participants' survey, which showed "voluminous documents required" as the main hurdle that prevents them from accessing financing opportunities. They also cited geographic barriers, with many LGUs located far from major lending institutions, and limited capacity to pay loans.

Priority COVID-19 projects of LGUs

- 36% Agri-fisheries (fisheries production, fish landing, value adding activities in the supply chain)
- 16% COVID testing center/improvement of isolation facility
- 14% Livelihood programs/opportunities
- 10% Enterprise Development (enabling SMEs)
- 04% Potable Water Supply Improvement
- 04% Infrastructure Investments
- 04% Mental Health
- 04% Education

Challenges and Barriers to Financing Access

- 24% Voluminous documents required
- 16% Distance between LGU and the financial institution
- 16% Lack of funds/capacity to pay
- 16% Long approval process
- 13% Lack of information about the program
- 05% Limited slots
- 05% Risk of acquiring the virus
- 05% Feedback/Communication

HEAL & RESPONSE Financing products

and Bank has created the Help via **Emergency Loan Assistance for LGUs (HEAL)** lending program to supplement the government's initiatives in fighting COVID-19 by providing direct support to vulnerable groups and individuals through local government units, according to Engr. Generoso S. David, LBP Assistant Vice President.

The amount of loans under HEAL will be based on the actual request of the LGU but should not exceed the BLGF computation of their net borrowing capacity. Mode of release can be staggered or lump sum, and credited to the borrower's account maintained with Land Bank.

Processing time depends on the amount of the loan. "If it's less than P50 million, the approval process will be a lot shorter... Based on our experience, *talagang napakaikli*, especially if the loan amount is P1 million, P2 million, P3 million — it only takes two weeks to process such kind of loans," said David.

Meanwhile, the DBP created the **Rehabilitation Support Program on Severe Events (RESPONSE)**

financing product even before the pandemic began, which can be used for COVID-19 recovery. Rustico Noli D. Cruz, Vice-President and Head of DBP's Program Development and Management Department, said the objectives of the program are to support the national government in rebuilding and expediting recovery process of calamity-stricken areas, and to extend credit assistance for rehabilitation. The program supports both public and private institutions regardless of size, and projects can be economic, social, and environmental in nature. Loans are credited to the LGU's DBP account.

Total processing time from application to release of funds is within 45 working days after the LGU's submission of complete pre-processing requirements to the DBP Account Officer, according to Cruz. However, he said the 45-day turnaround time is just a benchmark and the electronic submission of documents that has been allowed due to the pandemic could shorten the processing time.

The graphic features a circular logo for the Bureau of Local Government Finance (BLGF) with the year 1987 at the bottom. To its right is the logo for rare, featuring three stylized fish-like shapes in blue, green, and yellow. Below these logos is the text: "invite you to a Zoom Learning Session on".

Access to Financing Opportunities for Covid-19 LGU Recovery

Tuesday, 23 June 2020 | 9:30–11:30 AM

Rustico Noli D. Cruz
Vice President
Head, Program Devt & Mgmt 1 Dept
Development Bank of the Philippines

Ma. Pamela P. Quizon
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Land Bank of the Philippines

Comparison of HEAL & RESPONSE

RESPONSE by DBP

The general process involves five steps:

- Submission of pre-processing requirements by the LGU
- Processing of submitted documents
- Approval of proposed loan
- Documentation of approved transactions and post-approval requirements
- Release of loan proceeds through the LGU's deposit account in DBP

There are 12 pre-processing requirements:

1. Application Letter or Letter of Intent signed by the Mayor
2. Write-up of the LGU (including Disaster Risk Management System and Project Description)
3. Certified copy of the LGU's Comprehensive Development Plan
4. Customer Information Form
5. List of Sangguniang Bayan/Panlungsod members
6. List of referred creditors
7. Borrowing Resolution passed by the Sangguniang Bayan/Panlungsod
8. Certification from provincial/municipal treasurer that existing loan amortizations are regularly paid, and that total amortizations do not exceed 20% of the LGU's income
9. Last three years' COA-audited Financial Statement of the LGU
10. Seal of Good Financial Housekeeping
11. Certified copy of the LGU's Overall Performance Index
12. Project Documents (such as building plans and specifications, drawings)

Post-approval requirements are the following:

1. Monetary Board opinion issued by the Bangko Sentral ng Pilipinas
2. Certification of Debt Service and Borrowing Capacity from the Bureau of Local Government Finance
3. Certified copy of the DILG Seal of Good Financial Housekeeping
4. Ordinance/Validated Ordinance ratifying the approved terms and conditions of borrowings to be enacted by the LGU
5. Waiver of confidentiality on the LGU's deposits and investments
6. Proof of filing of ECC/CNC for projects

HEAL by LBP

The general loan process involves four steps (although this can be reduced to only three if the LGU avails of the bank's Omnibus Term Loan Facility);

- LBP Lending Center (LC) markets to LGUs
- LGU files a loan application with the nearest LC
- LC evaluates and processes the application and sends Notice of Approval to LGU
- LGU submits and complies with pre-release documents (list to be provided by the LBP Account Officer, along with post-release documents)

There are only three required pre-processing documents (in contrast to the usual 10):

1. Sanggunian Resolution – authorizing the local chief executive to enter into a loan agreement, sign loan documents, and approve the projects to be financed
2. Approved/Supplemental Budget for the current year
3. List of elected LGU officials and key officers

| Loan Product | HEAL (LBP) | RESPONSE (DBP) |
|-----------------------------------|---|---|
| Tenor | Up to 5 years (plus 1-year grace period) | Up to 15 years (inclusive of 3-year grace period) |
| Interest Rate (per annum) | 5% (fixed for term of loan) | 4–5% (fixed for 5 years) |
| Percentage of Project Cost | Up to 80% | Up to 100% |
| Acceptable collateral | Assignment of IRA (up to extent of loanable amount) | Assignment of IRA (with holdout on deposits equivalent to one quarter amortization) |
| Fees/Other Charges | Standard | Waived |
| Availability Period | Up to December 31, 2020 | Up to 1 Year from the date quarantine is lifted |

Finance follows function: BLGF and Bangko Sentral

The BLGF and the Monetary Board of the Bangko Sentral ng Pilipinas (BSP) play key roles in the loan application process before any funds are released to LGUs.

Ma. Pamela P. Quizon, Director of the BLGF, explained that the Local Government Code established a key principle of decentralized governance — “Finance Follows Function” or the 3Fs rule.

“It means that when local autonomy powers were given to the LGUs in 1992, you are now allowed to borrow. The limitation is not on the amount of borrowings but on the amount of debt servicing. *Kailangang 20 percent lang,*” Quizon said, “because our policymakers do not want to sacrifice your other public services. *Kailangan po kasing matugunan pa rin natin ‘yon.*”

The authorization of the local chief executive and the Annual Investment Plan form part of the regulations for loans, while the BLGF and Bangko Sentral determine the debt ceiling and borrowing capacity through two instruments:

1. The BLGF issues a certificate of Net Debt Service Ceiling and Borrowing Capacity (NDSCBC) after the LGU submits four documents for evaluation (see box). Due to pandemic restrictions, electronic submission to the regional office is now acceptable, Quizon said. Previously, BLGF required 12 documents as well as manual submission at the regional and central levels, but the process has been simplified “because it will give us three benefits: streamlining central controls, reducing compliance costs, and encouraging borrowings,” she added.

The regional office will make a preliminary computation before transmitting the documents to the BLGF central office, which will make the final computation and issue the NDSCBC certificate to the LGU. If the documents are complete, the BLGF can process the certificate in 15 working days or even less. “We’re making sure that we follow our rules. We are ISO-certified when it comes to processing debt servicing applications,” Quizon said.

2. The certificate is a key requirement for obtaining a positive Monetary Board opinion from Bangko Sentral. Quizon said this is necessary to make sure that the LGU loan “does not negatively affect money supply, inflation, and the national balance of payments.”

The Local Government Code allows LGUs to “create indebtedness and avail of credit facilities” for a wide range of purposes. According to BLGF, examples of projects that can be funded through credit borrowing by LGUs include:

- Capital investment projects (construction, improvement, and maintenance of public facilities; infrastructure facilities; housing projects; acquisition of real property)

- Livelihood and economic enterprises (agricultural, industrial, commercial, house financing)
- Property, plant, machinery, equipment (and necessary accessories)
- Self-liquidating, income-producing development or livelihood projects

Calculation of LGU Borrowing Capacity

1. **Debt Service Ceiling (DSC)**
 - $20\% \times \text{Annual Regular Income (ARI)}$

ARI: The average previous 3-year locally sourced income, *plus*
Other shares from national taxes (based on COA data), *plus*
Actual annual IRA (based on Department of Budget and Management data)
2. **Net Debt Service Ceiling (NDSC)**
 - DSC less All amortizations payable during the year)
3. **Borrowing Capacity (BC)**
 - NDSC \times Annuity Factor)

BLGF requirements for certificate of LGU borrowing capacity

1. Letter Request from the Local Chief Executive specifying:
 - Lending institution (LI)
 - Terms and conditions of the proposed loan (must be supported by an Offer Sheet from the LI, with the same amount of loan)
 - Purpose of the loan
2. Certification from the Local Treasurer indicating:
 - Types and purpose of loans and other obligations contracted
 - Name of the LI
 - Date of approval and maturity
 - Remaining balances of loans and other obligations
 - Annual amortization schedules from the LI
3. Annual Audit Certificate for the most recent year from the Commission on Audit
 - Showing no adverse findings against the LGU
 - Supported by year-end Financial Statements (with pre-closing trial balance and detailed Statement of Financial Performance)
4. Certification issued by the LI
 - Stating that it shall not require LGU deposits as compensating balance for the loan (for non-authorized government depository banks)

Why Borrow?

The country has 1,489 municipal LGUs as of 2019, according to data from the Philippine Statistics Authority. Borrowing is a key strategy in easing poverty and pump-priming the local economy. However, there are only about 200 LGUs with existing loans, Quizon noted.

"We have low levels of borrowing especially if we compare our borrowings to other developed countries. Our outstanding balance is less than 1 percent of the Gross Domestic Product that we have. In other developing countries, it has already reached 5 percent," she said.

Many LGUs are hesitant in mobilizing financial resources through borrowing due to the stigma attached to loans and the difficulties in preparing loan application requirements, according to Rommel Kirit, Program Implementation Manager of Rare.

"There is this perception that if you borrow or loan, whether it is secured or not, it will result in financial instability," noted Kirit. Even if LGU executives are aware of the problems in their locality and have some solutions in mind, "putting all these ideas into one comprehensive program is sometimes beyond the capacity of the staff of the local government units so much so that there is a difficulty in writing a project proposal to be submitted to lending institutions," he added.

Given the detrimental impact of COVID-19 on people's welfare, the BLGF and bank representatives urged the LGUs to think of the crucial role of loans in supporting their recovery plans.

"You can borrow and use the potential of borrowing to pursue projects for the development of your locality — *para maging vibrant ang economy ninyo, magkakaroon kayo ng job opportunities, mali-lift ninyo from poverty yung mga constituents ninyo*," said David from Land Bank.

This is especially true during periods of low-revenue generation, like now when LGUs are hard-pressed for funds but need to provide for testing centers, hospitals, and other support services to cope with COVID-19. David said loans could also be used for roads and telecommunication facilities that will encourage business to migrate to LGUs.

The pandemic has opened opportunities for more creative and adaptive problem-solving, said David. "This is really the time for us to really rethink — put our mindset into another perspective... Take this opportune time [to] develop really good projects... We want to finance projects or any undertaking that will lift you up, especially lift up your people from poverty," he added.

Cruz of DBP gave two main reasons why LGUs should consider credit financing, especially during the COVID pandemic. "It is very important that the LGU play its role in the pump-priming and thus investment is required," he said. "Second point is, the interest rate is low. It's really time to borrow for LGUs," he said.

"Huwag po kayong matakot mangutang. We are here to help," Cruz assured the LGUs at the webinar. "By the way, we [DBP and LBP] are also government, so we are allies here," he added.

Mayor Art Solante from Tudela in Cebu expressed interest in accessing credit for development projects, saying they were

already in the process of submitting documents to the BLGF when COVID quarantine restrictions were imposed. Tudela is a fifth-class municipality that is dependent on their Internal Revenue Allotment or IRA, valued at P63.9 million for 2020 and P68 million for 2021. "Kung 50 percent lang ang magamit na development fund, mahina ang development," he said. This is the reason why Tudela is considering a loan for the first time ever.

"We really need to borrow if only to finance our proposed development projects like opening up roads — farm-to-market roads -- for our farmers, because we are an agricultural town. [This is] for the farmers to be motivated to cultivate more idle lands, *lalo na ngayon* with the new normal, with the Balik-Probinsya program of our national government. We really intend to do these things through borrowing," said Mayor Solante.

Other LGU participants said even though they are interested in accessing credit, they are put off by technical requirements such as the project proposal and feasibility study that form part of the application.

Cruz said DBP has templates for project proposals that LGUs can use. As for more highly technical projects like water impounding systems with plenty of engineering requirements, the bank recommends that LGUs apply for design-build packages where the engineering design is built into the loan. This takes the burden of design away from the LGUs when applying for credit, he said.

Land Bank's David added that LGUs can also seek financing for feasibility studies or technical designs. Other "creative ways" that David suggested are asking for funds from the provincial government for the feasibility study, or getting a private entity that is willing to do the design for the LGU and be paid at a later date as a project partner.

Summing up the LGU participants' reactions, Vice Mayor Alfredo M. Coro II of Del Carmen, Surigao del Norte said the diversity of the projects that will be supported by the banks "allows LGUs to be more creative" in addressing the problems they are trying to resolve. "The LGUs recognize really the value of investing now, especially with the really good interest rates to address the much-needed public services. Definitely, loans are viable external funding," he added.

"If there are better ways of communicating — given our restrictions and uncertainties in the coming days... *baka makatulong po yung ating mga bangko at BLGF* in ensuring that much-needed financing desired by the local governments to pursue... sustainable solutions to what we are facing — *ay mapondohan po kaagad*," Coro said.

In response, Quizon said the BLGF is helping to address weak demand for borrowings by streamlining its process so that it will be easier for LGUs to apply for loans. The bureau is required to report weekly to the Office of the President on how many LGUs they have served, and wants the BLGF to fast-track loan approval and broaden access to credit financing.

"With the national government aggressively pushing forward to address massive infrastructure backlog and also to address this public health situation that we have now, this is a clear opportunity for us to complement the efforts at the national level with initiatives to stimulate more and better LGU capital investment," Quizon said.