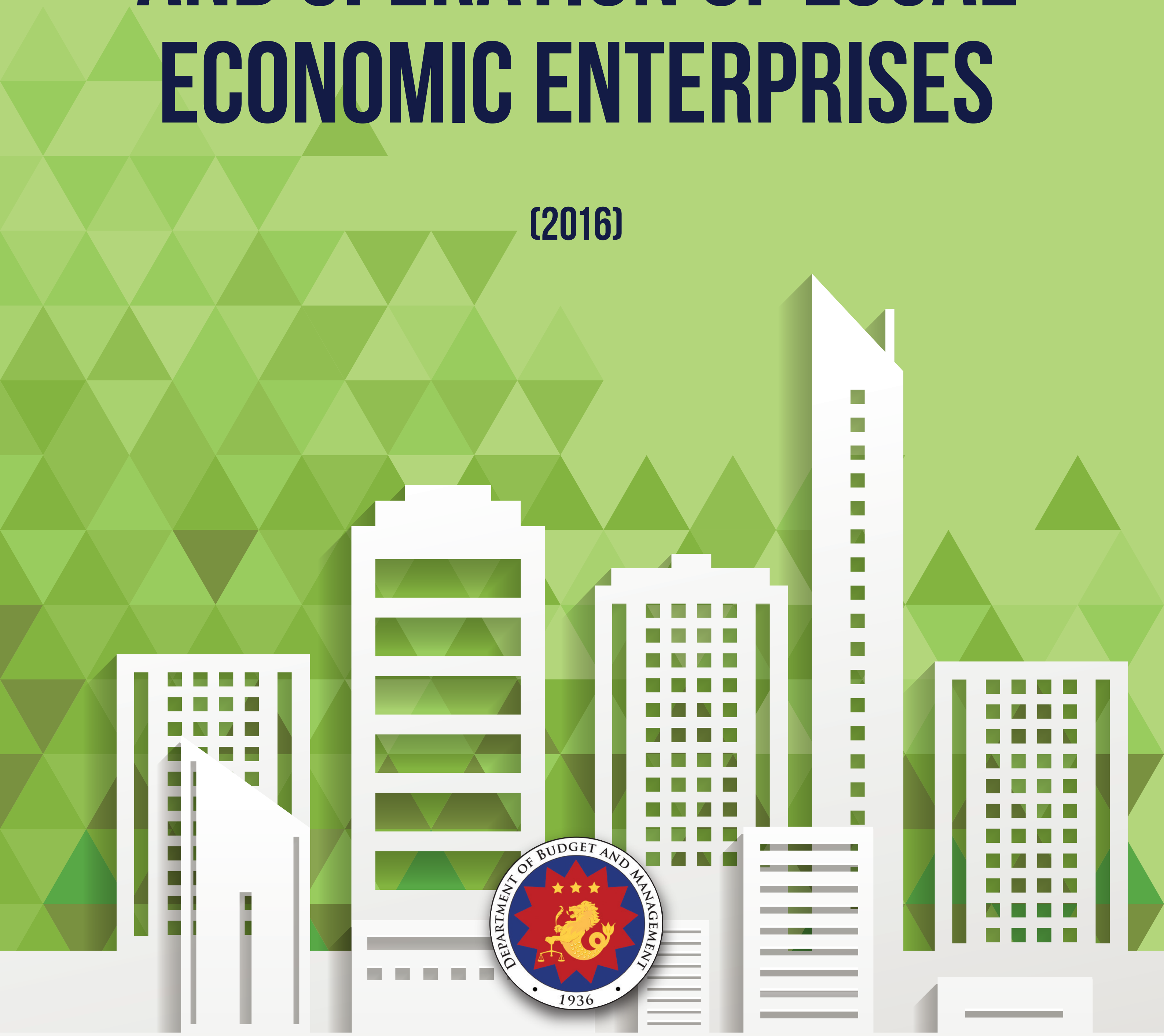
MANUAL ON THE SETTING UP AND OPERATION OF LOCAL ECONOMIC ENTERPRISES

(2016)



DEPARTMENT OF BUDGET AND MANAGEMENT

Message from the Secretary

The National Government, through the Department of Budget and Management, has relentlessly pursued reforms that will ensure *spending within means, investing in the right priorities*, and *delivering measurable results* within an environment that *empowers citizens* through greater transparency, accountability, and meaningful citizen's participation.

Parallel efforts have been taken at the local level consistent with the Local Government Units Public Financial Management (LGU PFM) Reform Roadmap and Implementation Strategy, which were formulated by the LGUs themselves.

Among the issues that the LGU PFM Reform Roadmap and Implementation Strategy seek to address is the proliferation of Local Economic Enterprises (LEEs), which are hobbled by inappropriate systems and practices that, in turn, result in losses.

The hefty subsidies required by the LEEs also eat into LGUs' coffers, thus, creating a negative impact on LGU finances. In response to this challenge, the LGUs proposed to develop a guide on how to set up and operate viable LEEs.

The Department of Budget and Management, in consultation with the other oversight agencies and the LGUs, developed the Manual for the Setting Up and Operation of Local Economic Enterprises (LEE Manual).

The LEE Manual is a practical guide to help LGUs decide whether or not to use LEEs as modes of service delivery. It encapsulates the state policies, rules and regulations affecting LEEs, and provides the detailed procedures for the establishment and operation of LEEs, including their divestment. It is an instructive "*how to*" guidebook, which can pave the way for LEEs that are relevant and self-sustaining.

I earnestly hope that LGUs will find it a useful and practical resource material as they work towards greater fiscal discipline and better delivery of public service.

Mabuhay at maraming salamat po!

Florencio B. Abad
Secretary

MANUAL ON THE SETTING UP AND OPERATION OF LOCAL ECONOMIC ENTERPRISES

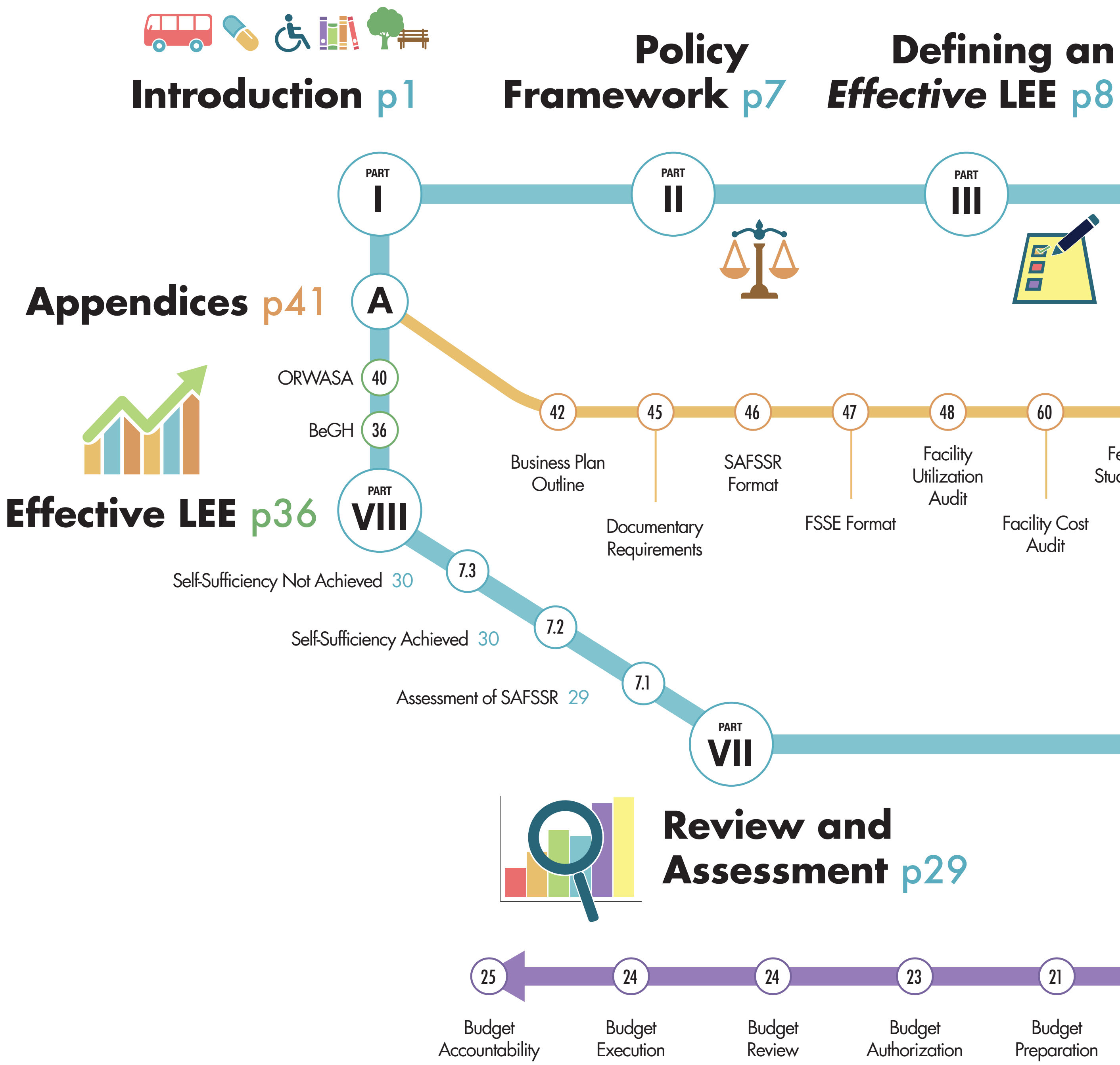
2016

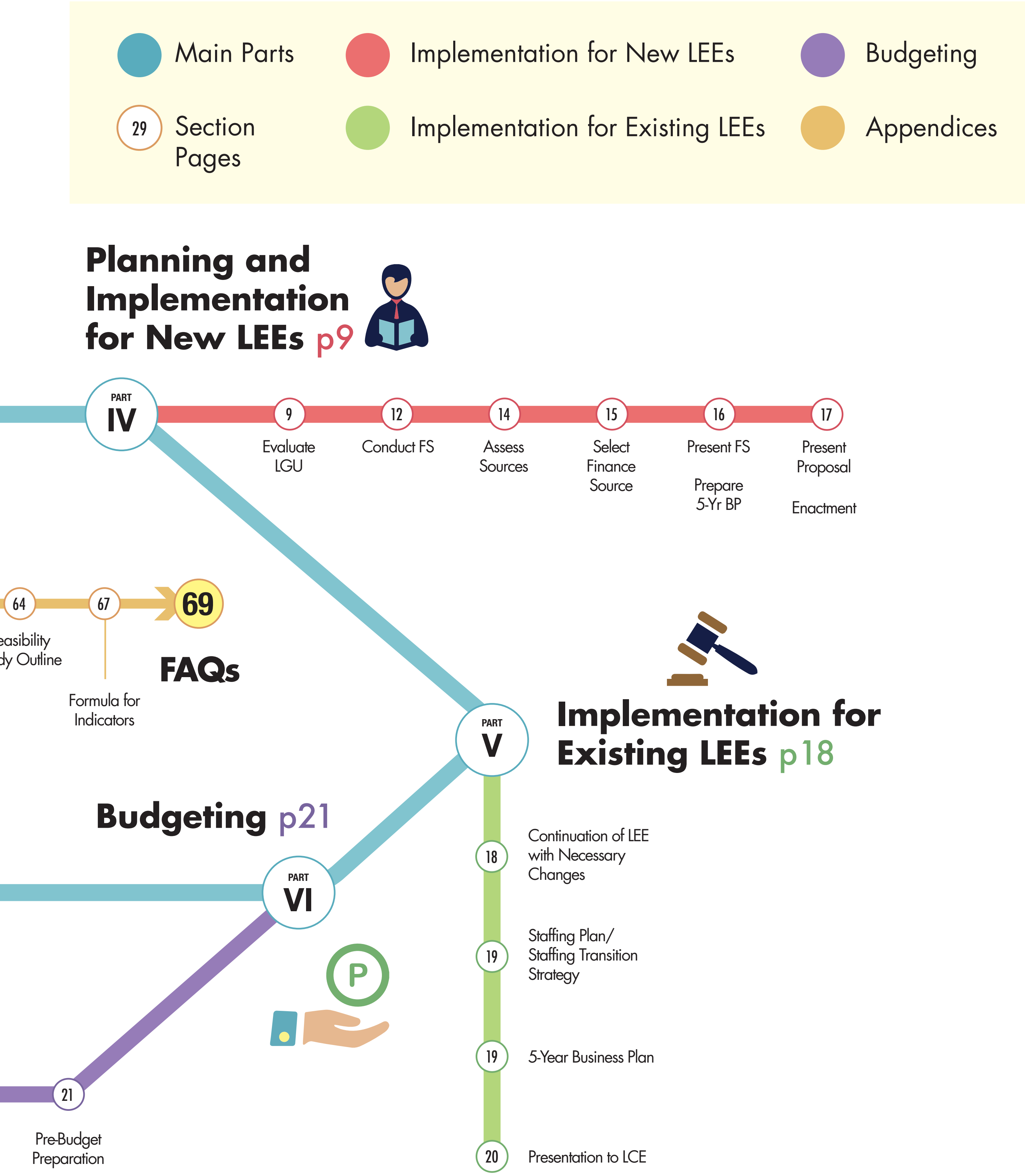
THIS MANUAL WAS DEVELOPED WITH SUPPORT FROM THE EUROPEAN UNION

UNDER THE PROJECT

“SUPPORT TO THE LOCAL GOVERNMENT UNITS
FOR MORE EFFECTIVE AND ACCOUNTABLE
PUBLIC FINANCIAL MANAGEMENT
(LGU PFM 2 PROJECT)”

SETTING UP AND OPERATION OF LOCAL ECONOMIC ENTERPRISES

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ACRONYMS AND ABBREVIATIONS

AO	Appropriation Ordinance
AOB	Annual Operating Budget
AIP	Annual Investment Program
APP	Annual Procurement Plan
ATP	Ability to Pay
BOM	Budget Operations Manual
BeGH	Benguet General Hospital
BOT	Build-Operate-Transfer
BLGF	Bureau of Local Government Finance
BP	Business Plan
CDP	Comprehensive Development Plan
CO	Capital Outlay
COA	Commission on Audit
COE	Current Operating Expenditures
CSC	Civil Service Commission
CSO	Civil Society Organization
DBM	Department of Budget and Management
DCF	Discounted Cash Flow
DENR	Department of Environment and Natural Resources
DOH	Department of Health
FS	Feasibility Study
FSSE	Financial Self-Sufficiency Evaluation
GSIS	Government Service Insurance System
HDMF	Home Development Mutual Fund
IAS	Internal Audit System
IRA	Internal Revenue Allotment
IRR	Internal Rate of Return
JICA	Japan International Cooperation Agency
LCE	Local Chief Executive
LDIP	Local Development Investment Program
LDRRMF	Local Disaster Risk Reduction Management Fund
LEE	Local Economic Enterprise
LEP	Local Expenditure Program
LFC	Local Finance Committee
LGC	Local Government Code
LGIAM	Local Government Internal Audit Manual

LGU	Local Government Unit
LPDO	Local Planning and Development Office
LWUA	Local Water Utilities Administration
MOOE	Maintenance and Other Operating Expenses
NAWASA	National Waterworks and Sewerage Authority
NEDA	National Economic and Development Authority
NGAS	New Government Accounting System
NGOs	Non-Governmental Organizations
NPV	Net Present Value
OB	Operating Budget
OEE	Other Economic Enterprises
ORWASA	Ormoc City Waterworks and Sewerage Authority
O&M	Operating and Maintenance
PED	Project Evaluation and Development
PDPFP	Provincial Development and Physical Framework Plan
PFM	Public Financial Management
PFMAT	Public Financial Management Assessment Tool
PHIC	Philippine Health Insurance Corporation
PPAs	Programs, Projects and Activities
PPP	Public-Private Partnership
PPMP	Project Procurement Management Plan
PS	Personal Services
PSA	Philippine Statistics Authority
PU	Public Utility
RA	Republic Act
RO	Regional Office
SAFSSR	Semi Annual Financial Self-Sufficiency Review
SOB	Supplemental Operating Budget
SSS	Social Security System
WTP	Willingness to Pay

1. INTRODUCTION

1.1. Background

Republic Act No. 7160, otherwise known as the Local Government Code of 1991 (LGC), mandates, as a primary operative principle of decentralization, the establishment of an accountable, efficient, and dynamic organizational structure and operating mechanism in the local government units (LGUs) that will meet the priority needs and service requirements of its communities.

As sanctioned by the LGC, the structure and operating mechanism may include the establishment and operation of local economic enterprises (LEEs). Many LGUs, however, fail to optimize this modality of service delivery.

Further, a review[1] of the performance of existing LEEs reveals that most operate at a loss and require heavy subsidies from LGUs since:

a. most are established for administrative and political reasons, e.g., accommodate a "bloated" LGU labor force and still remain within statutory budget ceilings; and

b. most operate on inappropriate systems and practices that fail to consider new know-how, local development priorities, and changing customer demands resulting in substandard quality and improperly priced public services.

Cognizant of the importance of LEEs in local development, the financial self-reliance of LEEs is a principal indicator for policy-based budgeting in the Public Financial Management Assessment Tool (PFMAT) for LGUs.[2] After all, well-planned and efficiently run LEEs can contribute to good local governance since they:

a. ensure that local public utilities and services meet constituency needs;

b. publish annual financial performance reports that provide transparency and accountability;

c. provide opportunities for citizen involvement; and

d. contribute to LGU revenue and resource mobilization because they could even generate modest financial surpluses through judicious control and tracking of LEE revenues and expenditures if properly set up and operated.

Given the LEEs' critical role in the LGU development and its effect to good local governance, the LGU public financial management (PFM) roadmap and its implementing strategy identified the "development of a detailed LGU guide for the setting up, operations, and divestment of LEEs" and "rollout with inter-agency support" as a key implementing strategy to effect the "linkage of budget planning to policy priorities," thus, this manual.

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1 Manasan, Rosario and Castel, Cynthia, Improving the Financial Management of Local Economic Enterprises, Philippine Institute for Development Studies Discussion Paper Series No. 2010-25 (Makati: October 2010). The study states that the less than business-like approach to local enterprise management has resulted in large arrearages and low collection efficiency and that the less-than-transparent reporting of the actual financial condition and profitability of these enterprises may have some adverse effect on decisions taken by LGU officials.

2 The PFMAT for LGUs is a self-assessment evidence-based instrument which describes the characteristics of an open and orderly PFM system. It is a diagnostic tool which establishes the indicators that will help the LGUs identify the strengths and weakness in their PFM system as bases for improvement measures.

1.2. Objectives of the Manual

The purpose of this manual is to provide an official guide to help LGUs:

a. decide whether to use LEE as the mode of public service and utility provision to its constituency;

b. conceptualize, plan, set up, and operate "purposeful" LEEs that effectively contribute to the attainment of their respective development goals and objectives; and

c. assess whether existing LEEs are viable and shall continue to operate.

This manual, which is instructive rather than mandatory, may also be used as a reference by oversight agencies, non-government organizations (NGOs), and civil society organizations (CSOs).

1.3. Local Economic Enterprises (LEEs)

This section presents a definition of LEEs, defining their underlying characteristics, their classification, and role in LGU development.

1.3.1. Definition of LEEs

LEEs are ventures wholly or partially owned by LGUs that generate revenue/income[3] through the sale of services and goods to meet a perceived constituency demand.

Section 17 of the LGC defines the basic services and facilities of the LGU. It, however, treats public utilities and economic enterprises separately. Economic enterprises are primarily concerned with public markets and slaughterhouses [Section 17(b)(2)(ix)], while the rest of the services and facilities are treated as utilities and services.

To quote pertinent portions of Section 17 of the LGC:

"Section 17. Basic Services and Facilities.

a. Local government units shall endeavor to be self-reliant and shall continue exercising the powers and discharging the duties and functions currently vested upon them. They shall also discharge the functions and responsibilities of national agencies and offices devolved to them pursuant to this Code. Local government units shall likewise exercise such other powers and discharge such other functions and responsibilities as are necessary, appropriate, or incidental to efficient and effective provision of the basic services and facilities enumerated herein.

b. Such basic services and facilities include, but are not limited to, the following:
xxx xxx xxx

(2) For a municipality:

i. Extension and on-site research services and facilities related to agriculture and fishery activities which include dispersal of livestock and poultry, fingerlings, and other seeding materials for aqua-culture; palay, corn, and vegetable seed farms; medicinal plant gardens; fruit tree, coconut, and other kinds of seedling nurseries; demonstration farms; quality control of copra and improvement and development of local distribution channels, preferably through cooperatives; inter-Barangay irrigation system; water and soil resource utilization and conservation projects;

3 The LGC defines "income" as referring to "all revenues and receipts collected or received, forming the gross accretions of funds of the LGU" [Section 306(i)] and "revenue" as referring to "income derived from the regular system of taxation enforced under authority of law or ordinance, and, as such, accrue more or less regularly every year" [(Section 306(m)]. This Manual, however uses revenue and income interchangeably to mean all types of income realized from the operations and activities of the LGU, or are received by it in the exercise of its corporate functions.

and enforcement of fishery laws in municipal waters including the conservation of mangroves;

ii. Pursuant to national policies and subject to supervision, control, and review of the DENR, implementation of community-based forestry projects which include integrated social forestry programs and similar projects; management and control of communal forests with an area not exceeding fifty (50) square kilometers; establishment of tree parks, greenbelts, and similar forest development projects;

iii. Subject to the provisions of Title Five, Book I of this Code, health services which include the implementation of programs and projects on primary health care, maternal and child care, and communicable and non-communicable disease control services; access to secondary and tertiary health services; purchase of medicines, medical supplies, and equipment needed to carry out the services herein enumerated;

iv. Social welfare services which include programs and projects on child and youth welfare, family and community welfare, women's welfare, welfare of the elderly and disabled persons; community-based rehabilitation programs for vagrants, beggars, street children, scavengers, juvenile delinquents, and victims of drug abuse; livelihood and other pro-poor projects; nutrition services; and family planning services;

v. Information services which include investments and job placement information systems, tax and marketing information systems, and maintenance of a public library;

vi. Solid waste disposal system or environmental management system and services or facilities related to general hygiene and sanitation;

vii. Municipal buildings, cultural centers, public parks including freedom parks, playgrounds, and sports facilities and equipment, and other similar facilities;

viii. Infrastructure facilities intended primarily to service the needs of the residents of the municipality and which are funded out of municipal funds including, but not limited to, municipal roads and bridges; school buildings and other facilities for public elementary and secondary schools; clinics, health centers and other health facilities necessary to carry out health services; communal irrigation, small water impounding projects and other similar projects; fish ports; artesian wells, spring development, rainwater collectors and water supply systems; seawalls, dikes, drainage and sewerage, and flood control; traffic signals and road signs; and similar facilities;

ix. Public markets, slaughterhouses, and other municipal enterprises;

x. Public cemetery;

xi. Tourism facilities and other tourist attractions, including the acquisition of equipment, regulation and supervision of business concessions, and security services for such facilities; and

xii. Sites for police and fire stations and substations and the municipal jail;

(3) For a Province:

i. Agricultural extension and on-site research services and facilities which include the prevention and control of plant and animal pests and diseases; dairy farms, livestock markets, animal breeding stations, and artificial insemination centers; and assistance in the organization of farmers' and fishermen's cooperatives and other collective organizations, as well as the transfer of appropriate technology;

ii. Industrial research and development services, as well as the transfer of appropriate technology;

iii. Pursuant to national policies and subject to supervision, control and review of the DENR, enforcement of forestry laws limited to community-based forestry projects, pollution control law, small-scale mining law, and other laws on the protection of the environment; and mini-hydro electric projects for local purposes;

iv. Subject to the provisions of Title Five, Book I of this Code, health services which include hospitals and other tertiary health services;

v. Social welfare services which include programs and projects on rebel returnees and evacuees; relief operations; and, population development services;

vi. Provincial buildings, provincial jails, freedom parks and other public assembly areas, and other similar facilities;

vii. Infrastructure facilities intended to service the needs of the residents of the province and which are funded out of provincial funds including, but not limited to, provincial roads and bridges; inter-municipal waterworks, drainage and sewerage, flood control, and irrigation systems; reclamation projects; and similar facilities;

viii. Programs and projects for low-cost housing and other mass dwellings, except those funded by the Social Security System (SSS), Government Service Insurance System (GSIS), and the Home Development Mutual Fund (HDMF), provided that national funds for these programs and projects shall be equitably allocated among the regions in proportion to the ratio of the homeless to the population;

ix. Investment support services, including access to credit financing;

x. Upgrading and modernization of tax information and collection services through the use of computer hardware and software and other means;

xi. Inter-municipal telecommunications services, subject to national policy guidelines; and

xii. Tourism development and promotion programs;

(4) For a City:

All the services and facilities of the municipality and province, and in addition thereto, the following:

i. Adequate communication and transportation facilities;

ii. Support for education, police and fire services and facilities;

xxx xxx xxx

j. To ensure the active participation of the private sector in local governance, local government units may, by ordinance, sell, lease, encumber, or otherwise dispose of public economic enterprises owned by them in their proprietary capacity.

Costs may also be charged for the delivery of basic services or facilities enumerated in this Section."

In Section 17(b) (2) (ix) of the LGC, note the words "and other" in the phrase "public markets, slaughterhouses, and other municipal enterprises". Also, Section 17(j) allows costs to be charged for the delivery of these services and facilities. These connote that all other LGU services and facilities in the list under Section 17(b) can be considered as economic enterprises, provided they generate income or revenues.[4]

On the other hand, Sections 313 and 325(a) of the LGC mention public utilities (PUs) separately from economic enterprises/other economic enterprises, but both are given the same treatment in these sections. This indicates that public utilities are classified as economic enterprises insofar as accounting and budgeting for these entities are concerned. However, the fact that public utilities are named differently and not lumped altogether with the other economic enterprises connotes that the former shall be given a different treatment in areas where such differentiation is warranted. This implies that PUs, due to their nature as discussed in item 1.3.2 of this manual, may be allowed to operate even if they may not earn enough income to cover their operations. This is in contrast to other LEEs that are expected to earn profits or at least recover costs.

To quote pertinent portions of Sections 313 and 325 of the LGC:

"Section 313. Special Accounts to be Maintained in the General Fund. Local government units shall maintain special accounts in the general fund for the following:

a. Public utilities and other economic enterprises;

b. xxx xxx xxx

"Section 325. General Limitations. - The use of the provincial, city, and municipal funds shall be subject to the following limitations:

a. The total appropriations, whether annual or supplemental, for personal services of a local government unit for one (1) fiscal year shall not exceed forty-five percent (45%) in the case of first to third class provinces, cities and municipalities, and fifty-five percent (55%) in the case of fourth class or lower, of the total annual income from regular sources realized in the next preceding fiscal year. The appropriations for salaries, wages, representation and transportation allowances of officials and employees of the <u>public utilities and economic enterprises owned,</u> operated, and maintained by the local government unit concerned shall not be included in the annual budget or in the computation of the maximum amount for personal services. The appropriations for the personal services of <u>such economic enterprises</u> shall be charged to their respective budgets."

Thus, in the Philippine context, LEEs are classified into two kinds: public utilities (PUs) and other economic enterprises (OEEs). As LEEs, both are modes of delivery of the goods and services to LGU constituents.

1.3.2. Public Utilities (PUs)

PUs are enterprises which are created by the Local Sanggunian through an ordinance for the purpose of providing an everyday basic necessity or service to the general public which otherwise cannot be provided adequately by the private sector. These LGU PUs shall be limited to:

a. LGU-operated water supply system not yet taken over by the Local Water Utilities Administration (LWUA);

b. power supply and distribution;

4 When an enterprise generates income, it simply means that it earns gross income, regardless whether it is able to recover its operating costs or earn net income.

c. telecommunications;

d. sanitation (local drainage, sewerage, solid waste collection and disposal); and

e. public transportation and transport terminals (bus, jeepney, parking, pier).

Unlike other economic enterprises, PUs by their very nature, may continue to be operated by LGUs even if the income they may generate may not be enough to sustain their operations. The provision of an everyday basic need of constituents that cannot be adequately provided by the private sector is a responsibility and an obligation of the LGU. However, PUs can be financially self-sufficient (100% cost recovery) or even earn net income when managed effectively.

1.3.3. Other Economic Enterprises (OEEs)

OEEs are LGU commercially operated establishments, which are created by the Sanggunian through an ordinance for the purpose of improving production and delivery of marketable goods and/or services for a specific market group. As such, they are expected to generate the bulk of their income from the sale of said goods and/or services. OEEs may include, but are not limited to:

a. public markets and shopping centers;

b. slaughterhouses, livestock trading and animal raising;

c. fish landing, ice plants and cold storage facilities;

d. post harvest facilities (grain storage, drying, milling);

e. commercial retail and office spaces;

f. public parks, sports and recreational facilities;

g. public cemeteries;

h. local hospitals; and

i. local colleges.

1.3.4. Role of LEEs in LGU Development

LEEs could play critical roles in LGU development. They could:

a. provide wider access to good and services with pricing that is affordable to a larger segment of the LGU population;

b. be a means to augment LGU revenues; and

c. attract investors by providing key services not provided by the private sector.

The LEEs are modes by which an LGU delivers goods and services to promote public welfare. However, when such goods and services are already being adequately provided by the private sector, the LGU concerned shall consider scaling down the LEE operations. In the development of its communities, the LGU shall not compete with but instead complement the private sector.

2. POLICY FRAMEWORK

The policy framework that serves as basis for the creation and operation of LEEs is primarily the LGC including related circulars intended to strengthen compliance to the relevant provisions of the LGC and related national laws.

The policies that guide the creation and operation of LEEs are Sections 3(b), 3(f), 3(l), 15, 17(a), 17(j),17(g), and 22(d) of the LGC.

Section 3(b) emphasizes the responsibilities of LGUs to set up appropriate service delivery structures and mechanisms to meet the basic needs of its constituents, to quote:

"Section 3(b). "There shall be established in every local government unit an accountable, efficient, and dynamic organizational structure and operating mechanism that will meet the priority needs and service requirements of its communities."

Section 3(f) provides for inter-LGU partnerships in the provision of services and facilities including joint ventures in LEEs, to quote:

"Section 3(f). Local government units may group themselves, consolidate or coordinate their efforts, services, and resources commonly beneficial to them."

The importance of private sector participation in LGU service delivery structures and mechanisms including LEEs is underscored in Section 3(l), to quote:

"Section 3(l). The participation of the private sector in local governance, particularly in the delivery of basic services, shall be encouraged to ensure the viability of local autonomy as an alternative strategy for sustainable development."

Section 15 lays down the basic functions of LGUs, to wit: (i) political subdivision of the national government of the Republic of the Philippines; and (ii) as a corporate body representing its constituency. As a corporate body, it can undertake business enterprises as a mode of production and delivery of goods and services to its constituents.

"Section 15. Political and Corporate Nature of Local Government Units. Every local government unit created or recognized under this Code is a body politic and corporate endowed with powers to be exercised by it in conformity with law. As such, it shall exercise powers as a political subdivision of the national government and as a corporate entity representing the inhabitants of its territory."

Pursuant to the above-quoted Section 17(a), the creation of LEEs can be considered as part of the exercise of LGU powers incidental to the efficient and effective provision of basic services and facilities. Under the basic operating principle of self-reliance, said Section also lays down basic LGU performance requisites for service delivery – efficiency and effectiveness.

"Section 17(a). Local government units shall endeavor to be self-reliant and shall continue exercising the powers and discharging the duties and functions currently vested upon them. xxx xxx xxx Local government units shall likewise exercise such other powers and discharge such other functions and responsibilities as are necessary, appropriate, or incidental to efficient and effective provision of the basic services and facilities enumerated herein."

Section 17(j) further empowers the LGU to sell, lease, encumber, or dispose of economic enterprises to the private sector. It also provides for various forms of private sector participation in LEEs – as creditor, investor, lessor/operator, property buyer, etc. At the same time, it allows LGU divestment of LEEs. The section also allows "service or facility" cost recovery via fees and charges for LEEs. Thus, both capital (including financing cost) and operating costs may be recovered through user charges.

"Section 17(j). To ensure the active participation of the private sector in local governance, local government units may, by ordinance, sell, lease, encumber, or otherwise dispose of public economic enterprises owned by them in their proprietary capacity."

Section 17(g) coupled with Section 17(j) implies that the LGU can subsidize LEEs as long as the services and facilities provided are covered under Section 17(b) and the LGU opts not to charge for the delivery for basic services and facilities.

"Section 17(g) xxx xxx xxx Any fund or resource available for the use of local government units shall be first allocated for the provision of basic services or facilities enumerated in subsection (b) hereof before applying the same for other purposes, unless otherwise provided in this Code."

"Section 17(j) xxx xxx xxx Costs may also be charged for the delivery of basic services or facilities enumerated in this section."

"Section 22(d). Local government units shall enjoy full autonomy in the exercise of their proprietary functions and in the limitations provided in this Code and other applicable laws."

3. DEFINING AN "EFFECTIVE" LEE

The policy framework defines an effective LEE to be one that contributes to the quality service delivery goals of the LGU. As such, an effective LEE must be designed, set up, operated, and managed in accordance with a well-prepared feasibility study and a detailed business plan that ensures the proposed LEE:

a. has clear vision, mission, goals, and objectives that fully respond to a particular constituency need;

b. supports the LGU development goals and objectives embodied in its Provincial Development and Physical Framework Plan (PDPFP) if it is a province or Comprehensive Development Plan (CDP) if it is a city/ municipality, and its corresponding Local Development Investment Program (LDIP) and Annual Investment Program (AIP);

c. augments and does not compete with goods and services provided by the private sector;

d. operates under the basic principle of financial self-sufficiency via cost recovery;

e. uses a performance-based approach with efficiency and effectiveness in service delivery as requisites; and

f. publishes annual performance reports that will provide accountability and transparency.

4. PLANNING AND IMPLEMENTING PROCEDURES FOR PROPOSED/NEW LEEs

This chapter will guide the LGU in deciding whether to use an LEE as a mode of production and/or delivery of goods and services to its constituents. It also provides the alternative modes of service delivery should an LEE be not feasible. This chapter provides the steps on how to plan and set up a new LEE.

The Local Chief Executive (LCE) may assign or designate the relevant local officials who will be responsible for planning for and implementing the new LEEs.

The steps are shown below:

4.1. Evaluate Whether the LGU Should Engage in LEE

The LGU shall study whether to engage in a particular LEE as the LEE shall be self-liquidating and must not represent a drain on the LGU's resources. The responsible officials will assess whether the establishment of the proposed LEE is warranted. The considerations that will guide the assessment are discussed next.

4.1.1. Marketable Good/Service

In keeping with its enterprise nature, the output – good or service – of the LEE must be marketable, that is, there is a measurable demand for it and that corresponding user charges may be levied on the use of the LEE output.

4.1.2. Feasibility Study-Based

a. An economic enterprise may be established after the conduct of feasibility study (FS) which shall show proof of its economic/social viability in the long term in terms of sufficient demand; and

b. that the prospective constituency users are able and are willing to pay for the use of the LEE output. This is established through ability-to-pay and willingness-to-pay surveys. The survey findings may form part of the FS.

4.1.3. "Hurdle" Criteria for the Appropriateness of an LEE

A set of hurdle criteria shall be satisfied to establish whether an LEE is the appropriate facility for the delivery of goods and services required by LGU constituents. The LEE shall:

a. (Criterion 1) satisfy both the economic and social objectives of the LGU as reflected in their PDPFP, in the case of the province, or CDP, in the case of city and municipality, and LDIP, as well as Annual Investment Program (AIP).

   The setting up and operation of a proposed LEE shall be included in development planning and investment programming. Thus, the annual slice of the funding requirements for a proposed LEE shall also be considered in the annual budget of the LGU.

b. (Criterion 2) fill gaps and services not adequately provided by the private sector and shall not compete with the private sector. The following points shall be clearly established:

   1. The LGU needs to play a primary role in the provision of the output proposed to be provided by the LEE; and

   2. The output of the LEE cannot be provided wholly or partly by the private sector.

   To illustrate, an LEE may be a public-private partnership wherein the LGU owns the enterprise although the operations are privatized. Since the LGU owns the LEE, it continues to play a primary role in the provision of the output.

c. (Criterion 3) operate as a business enterprise with its own Business Plan (BP) and budget. The provision of the LEE output shall be financially feasible to set up and operate given the existing budgetary and political realities within the LGU.

d. (Criterion 4) operate with appropriate staffing complement to satisfy its operating objectives.

   Human resources shall be in accordance with existing Civil Service Commission (CSC) rules and regulations. All personnel shall be hired on a contractual, casual and/or job-order basis. However, LGUs may assign regular staff on detail to the LEE during start-up operations.

   The LGU has the flexibility to create a unit (e.g., Economic Enterprise Unit) to be headed by a permanent staff that will supervise the operations and management of all LEEs, or place all LEEs under the Office of the Mayor, or other variants thereof.

   It is vital that each LEE be headed by a full-time manager responsible for the operations and management of the LEE. He/she will liaise closely with the LGU in obtaining the necessary regulatory permits and licenses during the pre-operation stage, and in providing the necessary feedback and reports during operations. A cashier properly deputized by the local treasurer and bonded by the Bureau of the Treasury shall take custody of the LEE finances.

Sources of information in determining whether the criteria are satisfied shall be included in the FS.

4.1.4. Alternative Modes of LGU Service Delivery

a. If Criteria 1 and 2 (Sections 4.1.3.a and 4.1.3.b of this manual) are not satisfied, then it simply means that:

   1. the service or good shall not be provided by the LGU; and

   2. the provision of the service or good shall be left to the private sector.

b. If Criteria 1 and 2 (Sections 4.1.3.a and 4.1.3.b) are satisfied but Criteria 3 and/or 4 (Sections 4.1.3.c and 4.1.3.d) are not, then the LGU shall consider the following options of partnering with the private sector or other LGUs:

   1. Contracting out the service provision via service, management, lease, and concession contracts;

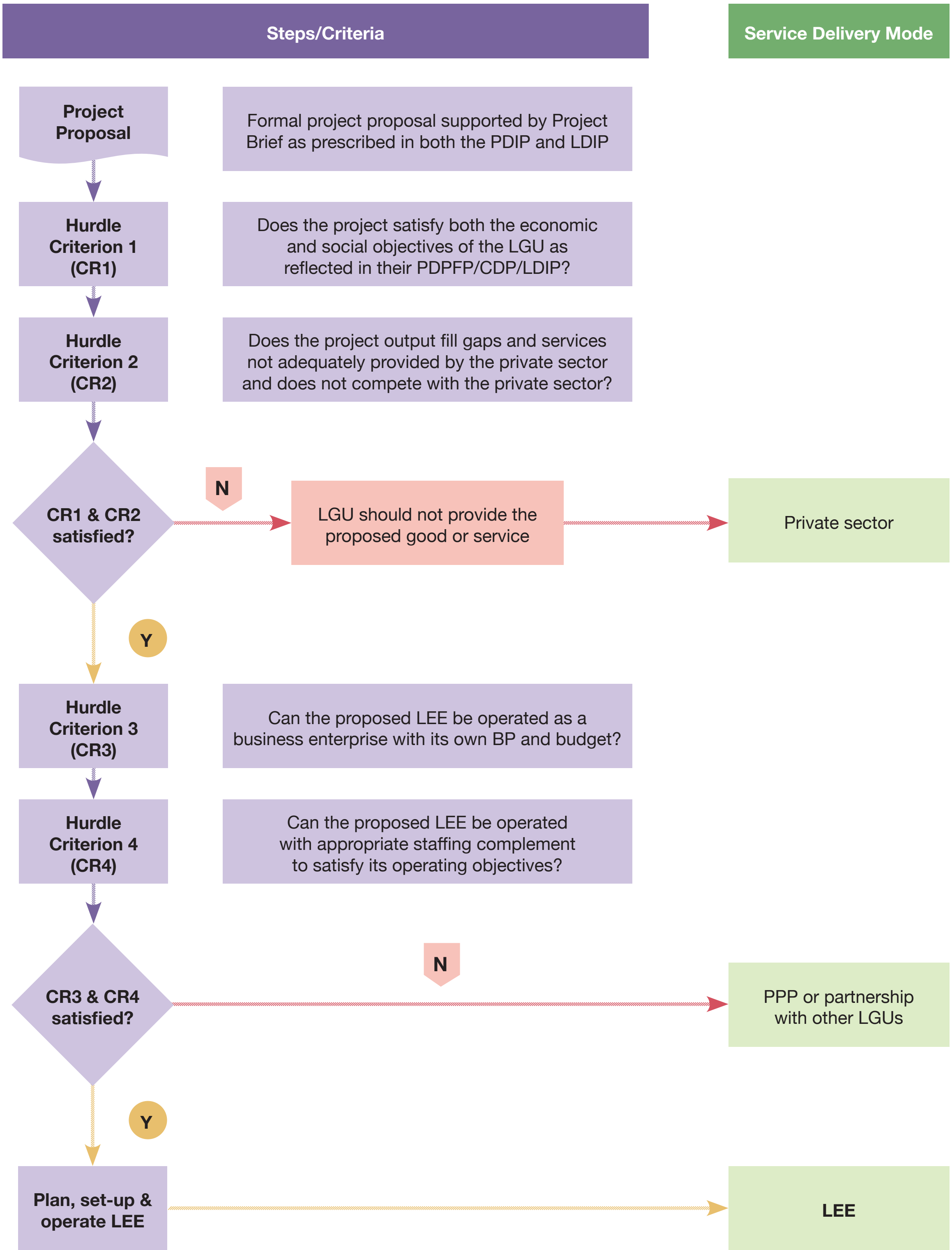
   2. Build-operate-transfer (BOT) and its variants;

   3. Joint ventures with other LGUs, private sector including NGOs and CSOs; and

   4. Inter-LGU partnerships.

   Figure 1 shows the process flow for LGU decision-making on the creation of LEEs.

Figure 1. Process Flow for LGU Decision-Making on the Creation of LEEs



4.2. Conduct a Feasibility Study for the Proposed LEE

An FS shall be conducted by the responsible officials in order to determine the viability of the proposed LEE. The FS will help in determining whether the proposed LEE is able to hurdle the criteria in determining if an LEE is the appropriate facility to deliver goods/services as set out in Section 4.1.3.

The LGU may opt to tap an external consultant for the study. Also, it may ask the services of a state university/college or another government agency that has the expertise in conducting FS in the area of business of the LEE. An FS shall be conducted for each proposed LEE.[5]

Generally, an FS has five (5) major components:

a. **Market Situation Analysis** – Establish the volume of demand and what the user-beneficiaries "can" and are "willing" to pay in terms of a combination of "user fees and charges" and "taxes" (the two cost recovery mechanisms for LGU projects and LEEs); identify competing products and services as well as potential target markets and customers; and position the LEE products or services against its competitors (or find a niche for the LEE products or services).

b. **Technical Analysis** – Based on the magnitude and nature of the demand for the LEE output, properly align the project scope, design, and specifications with the market situation; ensure that the project scope, design, and specifications have no adverse environmental impact; in cases where there are potential negative environmental effects, provide for mitigation (or compensation) in the project design and costs.

c. **Financial (Economic) Sustainability Analysis** – Establish financial viability in terms of adequate funds flow for the project cost and the subsequent annual operating and maintenance (O&M) costs since there is adequate cost recovery and sufficient financial (economic) incentives for the LEE; can also perform a formal but optional social benefit-cost analysis to establish the social desirability of the LEE.

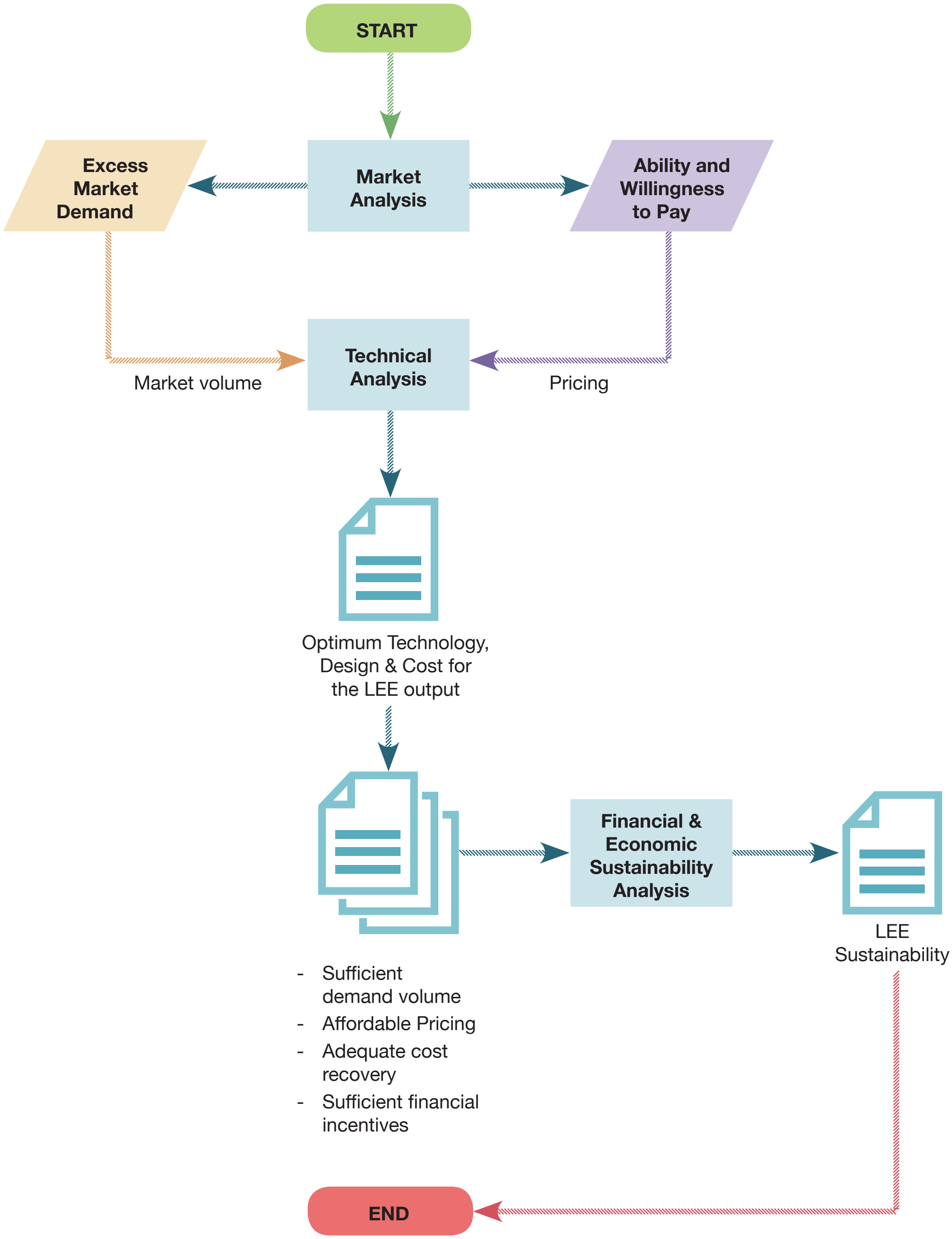
d. **Organizational Analysis** - Identify the organizational structure and manpower requirements needed to operate the LEE, including positions, qualifications, and job descriptions.

e. **Regulatory and Other Pre-Operational Requirements** – List down the necessary permits, leases, licenses, insurance, and other pre-operating requirements.

Figure 2 shows the process flowchart in conducting a feasibility study.

5 A good reference in the conduct of a project feasibility study is the Project Evaluation and Development Manual by the National Economic and Development Authority (NEDA).

Figure 2. Process Flowchart in Conducting a Feasibility Study



4.3 Assess Potential LEE Financing Sources

This section will help guide responsible LGU personnel in recommending which funding source will be tapped for the LEE. A reference that discusses financing sources that the LGUs may tap is the Resource Mobilization Manual by the Bureau of Local Government Finance (BLGF).

4.3.1 Current Available LGU Revenues

A major source of LEE financing is LGU revenues, which are composed of local taxes, fees and charges, revenues from existing economic enterprises, reserves, surpluses, and the Internal Revenue Allotment (IRA).

Transfers to LEEs shall take the form of subsidies or advances from the general fund (GF) pursuant to Section 313 of the LGC, subject to existing COA rules and regulations. These transfers, however, cannot be used to finance the personal services of LEE staff.

The annual operating budget (AOB) of the LEEs shall be included in the general fund annual budget (GFAB) of the LGU. The details of the AOB of the LEEs, however, shall be presented separately.

The pre-operating and initial operating fund requirements for newly established LEEs may be treated as subsidies or advances to be specifically appropriated by the local government concerned in its GFAB.

Unlike private corporations, LEEs cannot retain earnings derived during the current year. Since LEEs are maintained as special accounts (SA) in the GF, any excess of its income shall form part of the general fund pursuant to Section 313 of the LGC, to wit:

> "Local government units shall maintain special accounts in the general fund for the following: (a) Public utilities and other economic enterprises xxx xxx xxx Profits or income derived from the operation of public utilities and other economic enterprises, after deduction for the cost of improvement, repair and other related expenses of the public utility or economic enterprise concerned, shall first be applied for the return of the advances or loans made therefor. Any excess shall form part of the general fund of the local government unit concerned."

Thus, profits or income of the LEE shall first be used to defray the cost of improvement, repair, and other related expenses, then for paying back the advances given to the LEE. The excess then reverts to the GF.[6]

4.3.2 Borrowings

Borrowings include direct loans from government financial institutions and other government lending windows, local private and international lending institutions, and bond proceeds.

4.3.3 Foreign and Local Grants

Grants may come from both foreign and local sources, including national government funds for "hard" and "soft" development projects. Hard development projects refer to projects whose results are tangible assets such as capital outlays and other infrastructure projects. Soft projects pertain to those projects the results of which are not tangible, such as capacity building, systems improvement, and the like.

6 Funds provided to the LEE by the LGU cannot be treated as a loan since the LGU cannot provide a loan to itself.

4.3.4 Capital Income

Capital income is derived from the sales or use of existing LGU assets.

4.3.5 Cost Recovery Elements

The cost in establishing and operating the LEE shall be recovered through user fees and charges, and revenue-anticipating measures like special levies, and earmarked taxation of future benefits.

For example, under Section 240 of the LGC, a special levy can be imposed by an LGU on lands especially benefited by public works projects or improvements funded by the LGU, provided that the special levy shall not exceed 60% of the actual cost of such projects and improvements. The special levy takes the form of an additional real property tax imposed on the benefited properties. The imposition of a special levy requires the enactment of an enabling ordinance.

4.3.6 Cost Sharing

The LGU can share the cost in operating LEEs mutually beneficial to other parties, such as with other LGUs, the national government, or with the private sector.

4.3.7 Public-Private Partnerships

Private sector resources can be mobilized through public-private partnerships (PPPs) such as BOT and its variants, lease financing, and contractor/supplier credit, subject to existing guidelines issued for the purpose. All PPP ventures shall be subject to the applicable rules and regulations set by the PPP Center.

4.3.8 Donations

Donations from public and private entities are also another source of funding LEEs.

4.4 Select Financing Source

An analysis of the feasibility of each instrument to finance the investment cost of an LEE needs to consider the following factors and their corresponding guide questions, to wit:

4.4.1 Adequacy of Funds

Are funds adequate with respect to the LEE project's capital and pre-operating and initial operating maintenance and other operating expenses (MOOE) requirements?

4.4.2 Impact

What is the impact of the funding source or scheme on the community, including economic impact such as necessary "belt-tightening" measures and the deferment or even cancellation of other projects?

4.4.3 Political and Administrative Feasibility

Will increasing fees and tax rates to service debt requirements be politically and administratively feasible? Does the LGU possess the ability to prepare elaborate project documentation requirements such as FS?

4.4.4 Legality

Is the use of the funding source within the authority of the LGU?

4.5 Present the Feasibility Study Findings and Recommended Financing Source to the LCE

The responsible LGU personnel shall present to the LCE the FS results as well as the suggested funding source for the proposed LEE. The LCE has the prerogative to decide whether or not to create the proposed LEE based on the FS findings.

Should the LCE decide to proceed with the creation of the LEE, a business plan (BP) shall be prepared by the designated LGU personnel for the LEE. In case of two or more proposed LEEs to be created, each LEE shall have its own BP. The BP will spell out the implementing details of the LEE within a 5-year period.

4.6 If the LCE decides to create the LEE: Prepare a 5-Year Business Plan

A 5-Year BP for each LEE to be created shall be prepared by the designated LGU personnel or a duly hired external consultant. For new LEEs, the BP shall serve as a blueprint on how to make the operations of the LEE financially self-sufficient and eventually profitable.

The BP is the heart and soul of the operation of an LEE and the most important document that will be required by any lending institution or potential investor. It is a powerful management tool that details how the LEE is going to reach its objectives and where it plans to go in relation to where it is.

Moreover, some portions of the BP can be used to communicate to the LGU leadership, staff, and constituents the agenda for reaching the enterprise's goals; in training the staff and clarifying their roles and accountabilities in making the enterprise function successfully; and to attract capital and other resources.[7]

The initial BP for an existing LEE shall cover 5 years of operation. However, the BP is a dynamic plan and, as such, shall be reviewed and revised whenever needed, i.e., when market demand declines substantially due to unforeseen circumstances or when the technology used in the LEE becomes obsolescent and needs to be upgraded.

The sections found in the BP are as follows:

4.6.1 LEE Goals, Potentials, and Outlook

The BP shall identify the following; (a) goals of the LEE based on an analysis of the industry to which the LEE belongs; (b) consumption trends; and (c) economic forecasts or outlook for the industry.

4.6.2 Marketing Analysis and Plan

A marketing plan shall be formulated based on an analysis of the market. The marketing plan includes a profile of the target market, assessment of competitors, distinct advantages of the LEE's products or services, and marketing and sales strategies.

4.6.3 Management and Personnel Plan

The organizational structure and staffing requirements for the LEE forms a vital section of the BP. During the first year of operations, the LGU may detail some personnel holding permanent plantilla positions to the LEE to supervise and facilitate coordination and ease of compliance with the LGU regulatory requirements.

7 Covello, Joseph A and Hazelgren, Brian J. 2006. The Complete Book of Business Plans (Illinois: Sourcebooks Inc., 2006), 21-22.

The LEE personnel hired specifically for the LEE shall be on contractual status and/or on casual or job-order status. The performance of these personnel shall be evaluated periodically. If their performance falls below standards, these personnel can be replaced as practised in privately-owned ventures.

The LEEs shall follow the local regulations governing businesses but may be exempted from paying local regulatory fees if so desired by the LGU. However, in the course of LEE operations, the LGU and its personnel, in their official and personal capacities, shall not be exempted from paying user fees and charges due to the LEE facility in keeping with its economic nature.

Appendix A presents a detailed outline of a BP compliant with the usual requirements of commercial bank and development finance institutions.

4.7 Prepare and Present the Proposal for the Establishment of the LEE (Feasibility Study and Business Plan) to the Local Sanggunian as Basis for the Enactment of an Ordinance Creating the LEE

The LCE shall propose to the local Sanggunian the creation of the LEE. All the necessary documents particularly the FS and BP shall support the proposal. The LCE may present a draft bill for consideration of the local Sanggunian.

4.8 Enact the Ordinance Creating the LEE

The ordinance enacted by the Local Sanggunian shall contain, among others, the purpose and justification for the LEE, capitalization and sources of financing, organization and staffing, pricing policy, and sunset provision (provision mandating closure of the LEE if it has not achieved financial self-sufficiency over a specified period of time).

Figure 3 shows the process flow diagram for planning and implementing proposed/new LEEs.

Figure 3. Process Flow Diagram for Planning and Implementing Proposed/New LEEs

EVALUATE WHETHER THE LGU SHOULD ENGAGE IN LEE

↓

CONDUCT A FEASIBILITY STUDY (FS) FOR THE PROPOSED/NEW LEE

↓

ASSESS POTENTIAL LEE FINANCING SOURCES

↓

PROPOSE FINANCING SOURCES FOR THE LEE

↓

PRESENT THE FS FINDINGS & RECOMMENDED FUNDING SOURCE TO THE LCE

↓ If LCE decides to create the LEE

PREPARE A 5-YEAR BUSINESS PLAN (BP) FOR EACH LEE

↓

PRESENT TO LCE THE 5-YEAR BP FOR EACH LEE

↓

PREPARE THE PROPOSAL FOR THE ESTABLISHMENT OF THE LEE (INCLUDING APPENDED FS & BP) AND PRESENT TO THE LOCAL SANGGUNIAN AS BASIS FOR THE ENACTMENT OF AN ORDINANCE CREATING THE LEE

↓

ENACT THE ORDINANCE CREATING THE LEE

5. IMPLEMENTING PROCEDURES FOR EXISTING LEEs

5.1. Continue LEE Operations, but Make the Necessary Changes to Comply with the Legal Provisions and Other Requirements Governing LEEs

Existing LEEs shall be allowed to continue operating provided they comply with the legal provisions governing LEEs. These are discussed next.

a. Set up and maintain a special account in the GF for each LEE.

For the next budget period:

b. Exclude the salaries, wages, representation, and transportation allowances of LEE officials and employees from the GF budget.

c. Charge the appropriations for personal services of the LEEs against its own AOB.

d. Exclude the salaries, wages, and allowances of the LEEs in the computation of the maximum amount of personal services (PS) of the LGU.

e. Ensure that no LEE official or employee is allowed a salary rate higher than the maximum fixed for his position or other positions of equivalent rank.

f. Check that each LEE has its own separate AOB.

g. Include the programs, projects and activities (PPAs) of LEE(s) in the LDIP and AIP.

h. Apply the profits or income derived from the operation of LEE to:

    1. First, cost of improvement, repair, and related expenses of the LEE; and

    2. Second, return of advances received by the LEEs to the GF.

    3. Any excess shall form part of the GF.

i. Ensure the LEE AOB is included in the approved appropriation ordinance of the GFAB.

5.2. If Detailed Personnel are Assigned to the LEE: Prepare a 5-Year Staffing Plan and Staff Transition Strategy

Prepare a staffing plan featuring a transition strategy such that LGU personnel detailed (either full-time or part-time) to the LEE and concurrently working in other LGU departments would gradually be weaned out. The plan shall include the hiring of full-time staff in the management and operations of the LEE.

At the end of the 5-year period, the LEE shall be staffed by full-time personnel charged against the LEE budget.

5.3. Prepare a 5-Year Business Plan for Each LEE

The responsible staff or external consultant shall develop a detailed 5-Year Business Plan for the LEE.

For existing LEEs, a BP is mandatory to implement the necessary changes to comply with the legal requirements of LEEs as previously discussed in Section 5.1 and equally important, to make the operations of the LEE financially self-sufficient and eventually profitable. The BP shall cover all relevant facets of the LEE's operations including management, operations, staffing, risk analysis, marketing, and sales.

For existing LEEs with BPs, said BPs shall be reviewed and revised to conform to this Manual.

The BP is a dynamic plan, which shall be revised as needed, such as when market demand declines substantially due to unforeseen circumstances, or when the technology used in the LEE becomes obsolescent and needs to be upgraded.

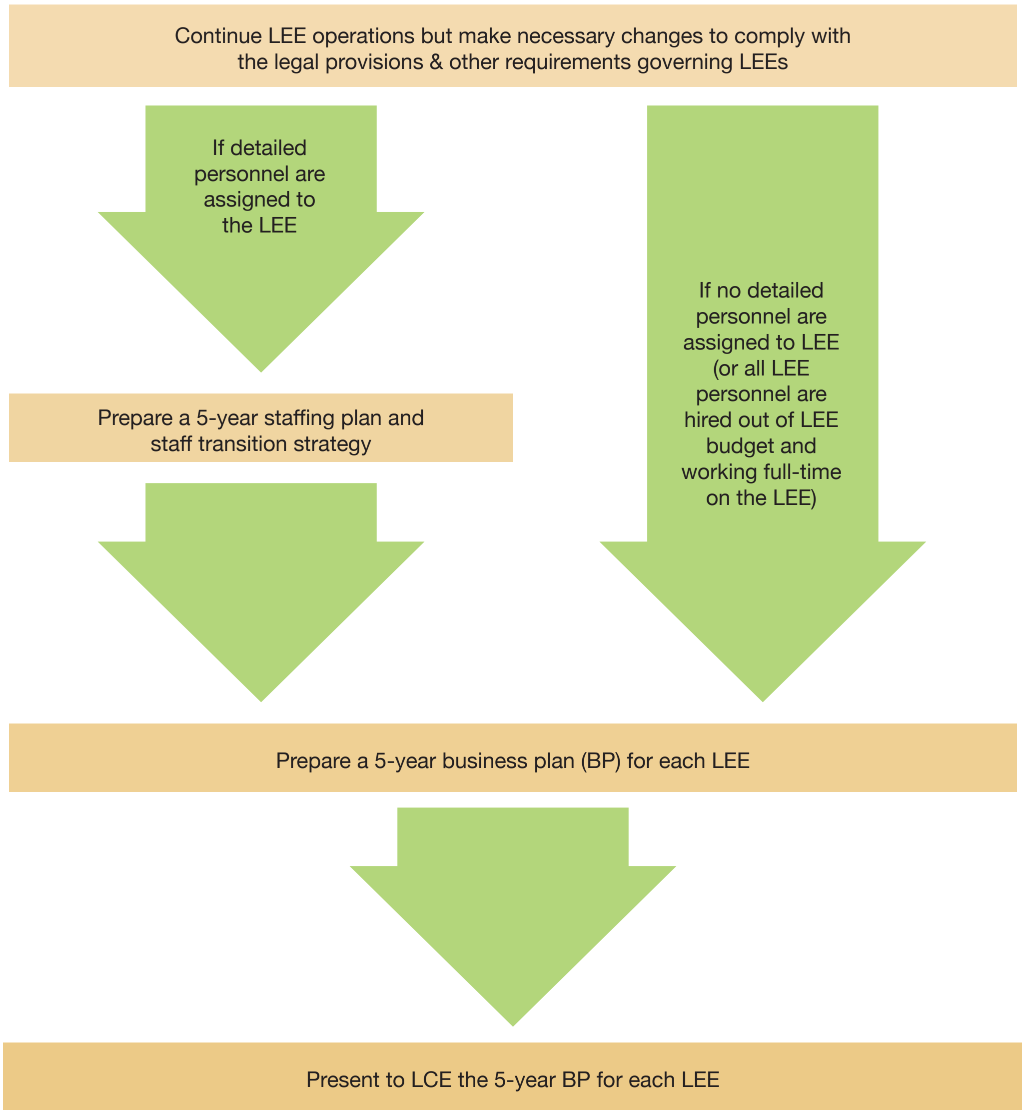
Appendix A shows a detailed outline for a BP that follows the usual requirements of commercial and development financing institutions.

5.4. Present to the Local Chief Executive the 5-Year Business Plan for Each LEE

The designated staff or external consultant shall present the 5-Year BP to the LCE and stress on the importance of directing the LEE operations towards financial self-sufficiency.

Figure 4 shows the process flow diagram of implementing procedures for existing LEEs.

Figure 4. Process Flow Diagram for Implementing Existing LEEs



6. BUDGETING FOR A LEE

The operations of a LEE shall be based on an annual operating budget (AOB) that is approved pursuant to the budget process provided for in the LGC and the Budget Operations Manual (BOM). The AOB, whether annual or supplemental shall, therefore, be covered by an approved appropriations ordinance, pursuant to the fundamental principle that, "No money shall be paid out of the local treasury except in pursuance of an appropriation ordinance or law." (Section 305(a) of the LGC)

In the case of the AOB, the same shall be included in the GFAB, and shall be authorized by the appropriation ordinance authorizing the latter.

6.1 Pre-Budget Preparation Activities

There are planning and programming activities that need to be undertaken before the start of the budget preparation phase pursuant to Section 305(i) and Section 305(g) of the LGC. To quote pertinent portions thereof:

> "Section 305(i). "Local budgets shall operationalize approved local development plans."
>
> "Section 305(g). "Local governments shall formulate sound financial plans and the local budgets shall be based on functions, activities and projects, in terms of expected results."

Pursuant to the foregoing Sections of the LGC, the plan to set up a new LEE or to continue an existing one shall have to be integrated in the local development plans of the LGU, which, in turn, shall have to be approved before the start of the budget preparation phase. In addition:

a. For Proposed/New LEEs

The viability of the proposed LEE shall be established through an FS and a corresponding BP for the LEE. The findings and recommendations of the FS and BP shall support the budget request for the proposed LEE.

b. For Existing LEEs

A BP and after the first year, the relevant semi-annual financial self sufficiency review (SAFSSR) reports, shall support the budget request for existing LEEs.[8]

6.2 Budget Preparation Activities

The following set of activities covers both new and existing LEEs.

6.2.1 Include in the Budget Call of the General Fund Annual Budget the Specific Guidelines for the Preparation of the AOB of LEEs

These specific guidelines shall include:

a. Objectives for the budget year, major thrusts, policy directions and strategies;

8 See Section 6.6.3 for a detailed 7 discussion of the SAFSSR.

b. Major assumptions used in estimating the revenue/income and expenditures for the budget year;

c. Estimated revenue/income and expenditure ceiling per LEE;

d. Expected output/results; and

e. Budget calendar and budget preparation forms as prescribed in the BOM.

6.2.2 Prepare and Submit the AOB of LEEs

a. Consistent with Section 317 of the LGC, the head/manager of the LEE shall prepare the budget proposal for the ensuing fiscal year and submit the same to the LCE through the local budget officer. However, if there is an existing Economic Enterprise Unit[9], the AOB shall first be reviewed by the said unit before it shall be submitted to the local budget officer.

b. The AOB shall reflect the estimated receipts of the LEE for the budget year and the corresponding expenditure program consisting of two (2) parts, namely: the current operating expenditures and the capital outlays, consistent with the LEE's submitted BP.

c. The estimates for the current operating expenditures and the capital outlays for the ensuing fiscal year shall also be consistent with the BP.

d. The end-user units of the LEE shall prepare the project procurement management plans (PPMP) for its different PPAs. These shall be reviewed and submitted by the LEE head/manager to the budget officer to support the LEE budget proposal. After the budget proposal has been approved by the LCE, the PPMP, as adjusted to conform to the LCE-approved budget proposal, shall be consolidated into a proposed annual procurement plan (APP) of the LEE for the budget year.

e. The following supporting documents shall be appended to the budget proposals of the LEEs:

  i. For proposed/new LEEs – FS and BP;

  ii. For existing LEEs - BP and after the first year, SAFSSR Reports.

6.2.3 Conduct Budget Hearings and Evaluate AOB Proposals of Each LEE

a. A separate budget hearing may be conducted for the LEE AOB.

b. The LFC shall initially evaluate the AOB of each LEE proposal as to its consistency with policies and priorities set forth in the budget call and its alignment with the BP.

c. The LFC shall spearhead the conduct of the budget hearing. Primarily, the budget hearing shall be undertaken for the purpose of:

  i. Rationalizing the existence of the LEE;

  ii. Determining the LEE's contribution to the development goals of the LGU as embodied in the CDP, LDIP, and AIP;

  iii. Validating the committed outputs and performance targets; and

  iv. Recomputing the estimates for current operating expenditures (COE) and capital outlay (CO).

9 A unit in the LGU which oversees all LEE operations.

6.2.4 Include the OB of each LEE in the Local Expenditure Program (LEP) that will be submitted to the LCE for Approval

The LEP shall be prepared in accordance with the guidelines and forms as prescribed in the BOM.

The estimated receipts of the LEEs shall be presented in the receipts program of the LGU, net of the subsidy from the GF. The expenditures of the LEE for the budget year shall likewise be presented in the expenditure program of the LGU, exclusive of the amount corresponding to the subsidy from the GF. The AOB shall provide the details of the receipts and expenditure programs of the LEE. It shall be annexed to the LEP, and shall form an integral part thereof.

6.2.5 Provide inputs pertinent to the AOB of LEEs for the Budget Message

The highlights, priorities and other necessary data and information pertaining to the LEE AOB shall be incorporated in the budget message for the GFAB.

6.2.6 Submit the LEE AOB to the Local Sanggunian

The LEE AOB shall be submitted to the local Sanggunian together with the GFAB not later than October 16 of the current year.

6.3 Budget Authorization

The LEE AOB shall be authorized together with the GFAB by the Sanggunian.

6.3.1 Enact the Appropriation Ordinance

a. Check the Budget Documents Submitted

The local Sanggunian, with the assistance of the LFC, shall check, for each LEE, the required documents, including the following appended documents:

i. For proposed/new LEEs - FS and BP;

ii. For existing LEEs - BP and after the first year, SAFSSR Reports.

b. Evaluate the AOB

The local Sanggunian, with the assistance of the LFC, shall evaluate the AOB of each LEE and validate the accuracy, reliability, and completeness of data and information on revenue/income and expenditures.

c. Deliberate on the AOB

The local Sanggunian shall deliberate on the LEE AOB as to its OB's consistency with the LGU plans and programs as contained in the AIP and the BP.

d. Authorize the AOB

After deliberation, the local Sanggunian shall authorize the AOB of each LEE as part of the appropriation ordinance authorizing the GFAB.

6.3.2 Approve the Appropriation Ordinance for LEE

The appropriation ordinance authorizing the GFAB, which includes the AOB of each LEE, shall be presented to the LCE for approval.

6.3.3 Submit the Appropriation Ordinance for Review

Within three (3) days after approval, the Secretary of the local Sanggunian shall forward to the reviewing authority copies of the approved appropriation ordinance for review.

6.4 Budget Review

The appropriation ordinance authorizing the GFAB, which includes the AOB of each LEE, shall be reviewed in accordance with the existing procedures in the BOM. In particular for LEE AOB, the following steps shall be undertaken:

6.4.1 Check the Appropriation Ordinance with the Appended Budget Documents

Using the checklist on documentary and signature requirements for the LEE annual and supplemental operating budgets for existing and proposed/new LEEs (Appendix B), the DBM Regional Office (RO) or Sangguniang Panlalawigan shall check the budget documents (with the required signatures) submitted together with the appropriation ordinance.

6.4.2 Review the Appropriation Ordinance

Check whether the LGU maintains a special account in the GF for the LEE.

a. Check whether the salaries, wages, representation, and transportation allowances of LEE officials and employees are excluded from the GF annual/supplemental budgets.

b. Check whether the appropriations for personnel services of the LEE are charged against its own AOB.

c. Check that the salaries, wages, and allowances of the LEE personnel are excluded in the computation of the maximum amount of personal services of the LGU.

d. Ensure that no LEE official or employee is allowed a salary rate higher than the maximum fixed for his position or other positions of equivalent rank.

e. Check that each LEE has its own separate AOB.

f. Check that the LEE is included in the LDIP and AIP.

g. Check that the profits or income derived from the operation of LEE are applied in the following order to:

    i. First, cost of improvement, repair, and related expenses of the LEE; and

    ii. Second, return of advances received by the LEEs to the GF.

h. Check that the budget for an LEE is authorized by the local Sanggunian through an appropriation ordinance.

i. Check that the AOB is presented separately for each LEE.

6.5 Budget Execution

The financial affairs, transactions, and operations of LGUs shall be governed by the fundamental principles provided under Section 305(a) to 305(g) of the LGC, as spelled out in the BOM.

The following are the steps in budget execution for LEEs:

6.5.1 Record the Approved Appropriation in the LEE's Books of Accounts

On the first business day of the fiscal year, the entire LEE AOB shall be recorded in the books of accounts.

6.5.2 Prepare Cash and Summary of Financial and Physical Performance Targets using the Prescribed Forms in the BOM

a. Prepare the cash program.

b. Prepare the Summary of Financial and Physical Performance Targets.

c. Prepare the detailed financial and performance targets.

d. Prepare the annual procurement plan (APP).

6.5.3 Obligate and Disburse Funds

Pursuant to the modified accrual system under the NGAS, obligations shall be taken up in the books of accounts as they are incurred. Accordingly, expenditures and obligations incurred during the fiscal year shall be taken up in the accounts of that year.

Obligations already incurred but not yet paid (accounts payable) shall be settled in accordance with existing budgeting, accounting, and auditing rules and regulations.

6.5.4 Adjust Cash Program for Shortages and Overages

The LEE, through its cashier, shall use the results of the cash flow analysis as basis for adjusting the cash program and the financial and physical targets.

The LEE shall compare its actual performance in both the financial and physical accomplishments vis-à-vis the targets for the quarter. If the actual financial performance is greater than the estimated cost, it means there is overspending beyond the available resources. It is indicative of inefficiency if the actual physical performance is below target. This needs corrective action.

6.6 Budget Accountability

Budget accountability is essentially accounting for the performance of the LEE in terms of revenue/income generation and resource utilization for the delivery of goods and services. It encompasses the recording and reporting of estimated and actual revenue/income and expenditures as well as monitoring and evaluation of the LEE performance vis-à-vis prescribed standard/policies and planned targets. Basically, it is the evaluation of the LEE performance in the execution of its annual and supplemental OBs.

The specific steps that shall be undertaken by the LGU shall be as follows:

6.6.1 Monitor Revenue/Income and Expenditure

The LEE AOB is accounted for on the first day of the fiscal year. The estimated revenue/income and expenditures in amounts approved and reviewed are recorded in the books of accounts where they shall be compared with the actual collections and disbursements for the same period.

Expenditures are tracked and monitored vis-à-vis the outputs and accomplishments.

Each LEE shall maintain its own book of accounts. The book of accounts will serve as a major source of information during the SAFSSR for each LEE, to be conducted by the designated LGU staff or duly hired external consultant.

6.6.2 Prepare and Submit Physical and Financial Reports to the LCE and Local Sanggunian through the LFC

The LEE Manager shall prepare the following reports to the LFC, who in turn, shall review the documents and submit these to the LCE and local Sanggunian. These LEE reports shall form part of the physical and financial reports of the LGU.

a. Physical Report: Physical Report of Operations

b. Financial Reports:

   i. Statement of Income and Expenses;

   ii. Cash Flow Statement;

   iii. Schedule/Aging of Accounts Payable;

   iv. Schedule/Aging of Accounts Receivable; and

   v. Other financial reports that may be required by oversight agencies.

6.6.3 Conduct Semi-Annual Financial Self-Sufficiency Review (SAFSSR) of each LEE and prepare SAFSSR Report

The SAFSSR is in compliance with Section 316(h) of the LGC which requires the LFC to conduct semi-annual review and general examination of cost and accomplishments against performance standards.

For existing/old LEEs, the first SAFSSR shall be conducted six months after instituting the necessary changes to comply with legal provisions and other requirements as discussed in Section 5.1.

In the case of a newly created LEE, the first SAFSSR shall be conducted six months after the start of its operation.

The objective of the SAFSSR is to determine whether the LEE is proceeding towards financial self-sufficiency (or 100% cost recovery) and according to the BP. The operations of a financially self-sufficient LEE shall be funded out of its sources rather than from the GF.

An LEE is considered self-sufficient if all the costs of operating the LEE are recovered 100%. The costs of operating the LEE include personnel services (PS), MOOE, and finance charges (interest expense).

The following shows the steps involved in performing the SAFSSR.

a. Collect from the LEE all supporting materials pertinent to the review. These include:

   i. Physical Report of Operations

   ii. Statement of Income and Expenses sourced from the local accounting office

   iii. 5-Year BP covering the period under review

b. Compute the true cost of operating the LEE. This involves a careful and thorough examination of costs in order to identify which costs shall be properly attributed to the LEE and which costs shall be attributed to the GF.

All resources required to produce the LEE good or service must be included in the cost. To identify all resources used to provide a good or service, all areas of local government activity must be examined to determine which are used in some way to provide the LEE goods or services.

In cases where the LEE officers and staff are detailed personnel who are also doing concurrent work in an LGU unit, proper attribution of costs shall be done depending on the time spent between at the LEE and at his/her LGU unit.

For example, if a staff of the Treasurer's Office divides his time between the public market (which has been classified as an LEE) such that he spends three days per week in the public market and two days a week in the Treasurer's Office, then his salary can be attributed as follows:

a. Charged against the LEE: monthly salary multiplied by 60% (or 3 out of 5 days per week) and

b. Charged against the GF: monthly salary multiplied by 40% (or 2 out of 5 days per week).

The other costs shall also be properly computed in order to come up with the true cost of operating the LEE.

c. Compute the revenues generated by the LEE.

d. Compute the net profit or net loss.

Appendix C shows the format for the SAFSSR report that shall be prepared by for each semi-annual period. The SAFSSR report shows total income, total expenses, net income, financial self sufficiency ratio (derived by dividing total income by total expenses multiplied by 100), and a textual analysis including the reasons for the financial results. The analysis may include the results of the physical report of operations, trends in income and expenses, and pertinent provisions in the BP. To the SAFSSR report shall be attached a copy of the Statement of Income and Expenses from the local accounting office for easy reference of detailed financial data.

The SAFSSR reports shall be compiled since these will be summarized at the end of the 5th year (since instituting the necessary changes to comply with legal requirements in the case of existing LEE or since the start of operations in the case of new LEE). The reports will be used to evaluate whether the LEE shall be allowed to continue its operations.

6.6.4 Present SAFSSR Report to the LCE and Local Sanggunian

The responsible local staff shall submit and present each SAFSSR report to the LCE and local Sanggunian. Copies shall be furnished to the LEE manager who shall use the results of the reports in improving LEE operations.

Shown as Figure 5 is the process flow diagram for budgeting LEEs.

Figure 5: Process Flow Diagram for Budgeting LEEs

Existing LEEs

PRE-BUDGET PREPARATION:
Include LEE in the AIP. Use findings of appended BP & after the first year, semi-annual financial self-sufficiency review (SAFSSR) report to support budget request for continuous operations of the LEE

New LEEs

PRE-BUDGET PREPARATION:
Include LEE in the AIP. Use findings of appended FS & BP to support budget request for new LEE.

BUDGET PREPARATION:
1. Include in the budget call of the general fund annual budget the specific guidelines for preparation of LEE AOB
2. Prepare and submit LEE AOB
3. Conduct budget hearings and evaluate LEE AOB proposal
4. Include the LEE AOB in the LEP that will be submitted to the LCE for approval
5. Provide inputs pertinent to the LEE AOB for budget message
6. Submit the LEE AOB to the local Sanggunian

BUDGET AUTHORIZATION:
1. Enact the appropriation ordinance
2. Approve the appropriation ordinance for LEE
3. Submit the appropriation ordinance for review

BUDGET REVIEW:
1. Check the appropriation ordinance with the appended budget documents
2. Review the appropriation ordinance

BUDGET EXECUTION:
1. Record the approved appropriation in LEE's books of accounts
2. Prepare cash & summary of financial & physical performance targets using prescribed forms in the BOM
3. Obligate & disburse funds
4. Adjust cash program for shortages and overages
5. Provide corrective measures for negative deviations

BUDGET ACCOUNTABILITY:
1. Monitor income & expenses
2. Prepare & submit physical & financial reports to the LCE & local Sanggunian through the Local Finance Committee (LFC)
3. Conduct SAFSSR of each LEE and prepare SAFSSR report
4. Present SAFSSR report to the LCE & local Sanggunian

7. REVIEW AND ASSESSMENT OF LEEs

A review and assessment of LEEs shall be done every five years. In the case of existing LEEs, the review will start five years after instituting changes to comply with the legal provisions governing LEEs. In the case of new LEEs, the review and assessment will commence five years after the start of its operations. Review and assessment activities shall help the LGU determine whether to continue, modify, expand, scale down, or close the LEE operations.

The following are the steps:

7.1. At the End of Each 5-Year Period, Prepare the FSSE Report and Decide Whether the LEE Should Continue its Operations

At the end of each 5-year period,[10] a decision shall be made whether the LEE has achieved financial self-sufficiency (or 100% cost recovery) and shall be allowed to continue operating. The preparation of the FSSE will signal the start of the review and assessment process. The FSSE shall use the 10 SAFSSR reports for the 5-year period, statement of income and expenses (with detailed income and expense items) from the local accounting office, and the relevant BP.

The designated LGU staff or consultant shall be responsible for preparing the FSSE Report and coming up with an analysis on the financial self sufficiency situation of the LEE as well as recommendation on whether or not the LEE shall continue to operate and other related actions. The FSSE findings shall be submitted and presented to the LCE and local Sanggunian to serve as basis in coming up with a decision on whether to continue LEE operations.

Appendix D shows the format for the financial self sufficiency evaluation (FSSE) report. The FSSE report:

- summarizes side by side the SAFSSR findings for the past 10 semi-annual periods (period of five years covered by 10 SAFSSR Reports);
- computes the cumulative totals of income and expenses for the past 10 semi-annual periods;
- determines the financial self sufficiency ratio of the LEE (Total Income divided by Total Expenses multiplied by 100);
- provides an explanation or analysis of the LEE's financial self-sufficiency situation; and
- recommends whether the LEE shall continue to operate and related actions.

The FSSE results shall yield either one of two alternative findings:

10 Five years correspond to half the usual 10-year LGU loan repayment period granted by creditor banks. It is envisioned that by halfway along the 10-year period, the LEEs should already be self-supporting to be able to repay its operating expenses including debt service.

a. Financial self-sufficiency or situation of 100% cost recovery and/or net income is achieved at the end of the 5-year period (see 7.2 of this manual); and

b. Financial self-sufficiency is not achieved at the end of the 5-year period or situation of less than 100% cost recovery and net loss (see 7.3 of this manual).

7.2. Financial Self-Sufficiency is Achieved at the End of the 5-Year Period (Situation of 100% Cost Recovery and/or Net Income)

If at the end of the 5-year period, the LEE registers 100% cost recovery and/or net income, the following steps shall be undertaken:

a. Continue LEE operations.

b. Continue to prepare SAFSSR Reports as discussed in 6.6.3 of this manual.

c. At the end of the 5-year period, prepare the FSSE Report in accordance with 7.1 of this manual.

7.3. Financial Self-Sufficiency is Not Achieved at the End of the 5-Year Period (Less than 100% Cost Recovery or Net Loss)

If at the end of the 5-year period, the LEE registers less than 100% cost recovery or a net loss, the designated LGU staff or duly hired consultant shall undertake the following steps:

a. Conduct a facility utilization audit [including a willingness-to-pay (WTP) study] to see whether the LEE's facilities and services can be improved to increase facility patronage and how it can be done. Appendix E shows the important considerations in doing a facility utilization audit.

b. Conduct a facility cost audit to determine the true cost of running the LEE (Appendix F).

c. Use the results of the facility utilization and facility cost audits to determine if the LEE shall continue its operations. The LEE shall continue operating if all of the following three (3) conditions are present:

   i. LEE services/products and facility patronage can be improved;

   ii. Facility users are willing and able to pay higher user fees that will cover the true cost of running the LEE; and

   iii. Increase in rates to recover the true cost of operating the LEE is socially and politically acceptable.

d. If all of these three (3) conditions for continued LEE operations are present, the LGU staff or duly hired consultant shall recommend the continued operations of the LEE and undertake the following:

   i. Prepare a 5-Year BP including sustainability strategies covering the next five (5) years. The BP can include the following strategies:

      (a) Improving facilities and services;

      (b) Intensifying information dissemination or promotions;

      (c) Increasing user fees that will cover the true cost of LEE operations and which amount customers are willing and able to pay based on the results of the WTP study;

(d) Automatically indexing user fees to inflation rates. An example is automatically adjusting every three (3) years the level of increase in user fees based on the level of increase in the regional inflation rate as published by the Philippine Statistics Authority (PSA);[11]

(e) Reducing cost by taking out undue charges like people working in other LGU departments but are charged against LEE funds; and

(f) Implementing changes in organizational structure and/or letting go and/or hiring new personnel.

ii. Prepare, submit, and present the facility utilization audit report, facility cost audit report, and 5-Year BP to the LCE and local Sanggunian.

iii. Continue LEE operations.

iv. Implement the 5-Year BP starting the succeeding year.

v. Continue to prepare SAFSSR reports as discussed in 6.6.3 of this manual.

vi. At the end of the 5-year period, prepare the FSSE report in accordance with 7.1 of this manual.

e. If not all of the conditions for continued LEE operations (discussed earlier in 7.3.c of this manual) are present, the designated LGU staff or consultant shall recommend an exit strategy specific to the LEE, outlining the desired conditions and terms. The exit strategies include:

i. Service shedding (i.e., LGU stops the production/provision of selected LEE goods/services to concentrate on a few LEE goods/services);

ii. Closure (i.e., LGU shuts down LEE operations completely; however, provision of products/services may be continued through another mode other than LEE); and

iii. Divestment (i.e., the LGU relinquishes either operational control or ownership to another entity). Privatization is the usual mode of divestment. In relinquishing control, management can be bid out to a private entity which is usually required to pay minimum guaranteed annual or monthly payment. In relinquishing ownership, the LGU sells the LEE to another entity.

After divestment, no LGU official or employee or their spouses and relatives within the fourth civil degree of consanguinity or affinity, shall be allowed to be a substantial stockholder or member of the Board of Directors or officer or owner of the corporation or to have substantial interest or be a partner in the business, pursuant to the Rules Implementing RA 6713.[12] The LCE shall ensure that this prohibition shall be expressly incorporated in the terms and conditions of the sale of the LEE.

In case of closure or divestment through relinquishing of ownership, an AOB for the succeeding year will no longer be needed

The studies required of an LEE are interrelated. The FS is required of a proposed/new LEE in order to determine its potential for cost recovery. If there is potential, the 5-Year BP is needed to show how this potential can be realized and how the LEE shall operate to attain financial self sufficiency. The facility utilization and facility cost audits meanwhile may be regarded as the counterpart FS for an existing LEE. These audits will help determine whether the existing LEE should be allowed to continue its operations.

11 The Philippine Statistical Authority determines and releases the official national and regional inflation rates. The automatic indexation of rates to the official regional inflation rate after a given number of years should be stipulated in the relevant Ordinance.

12 Code of Conduct and Ethical Standards for Public Officials and Employees.

Shown as Figure 6 is the process flow diagram for the review and assessment of LEEs.

Figure 6: Process Flow Diagram for Reviewing and Assessing LEEs

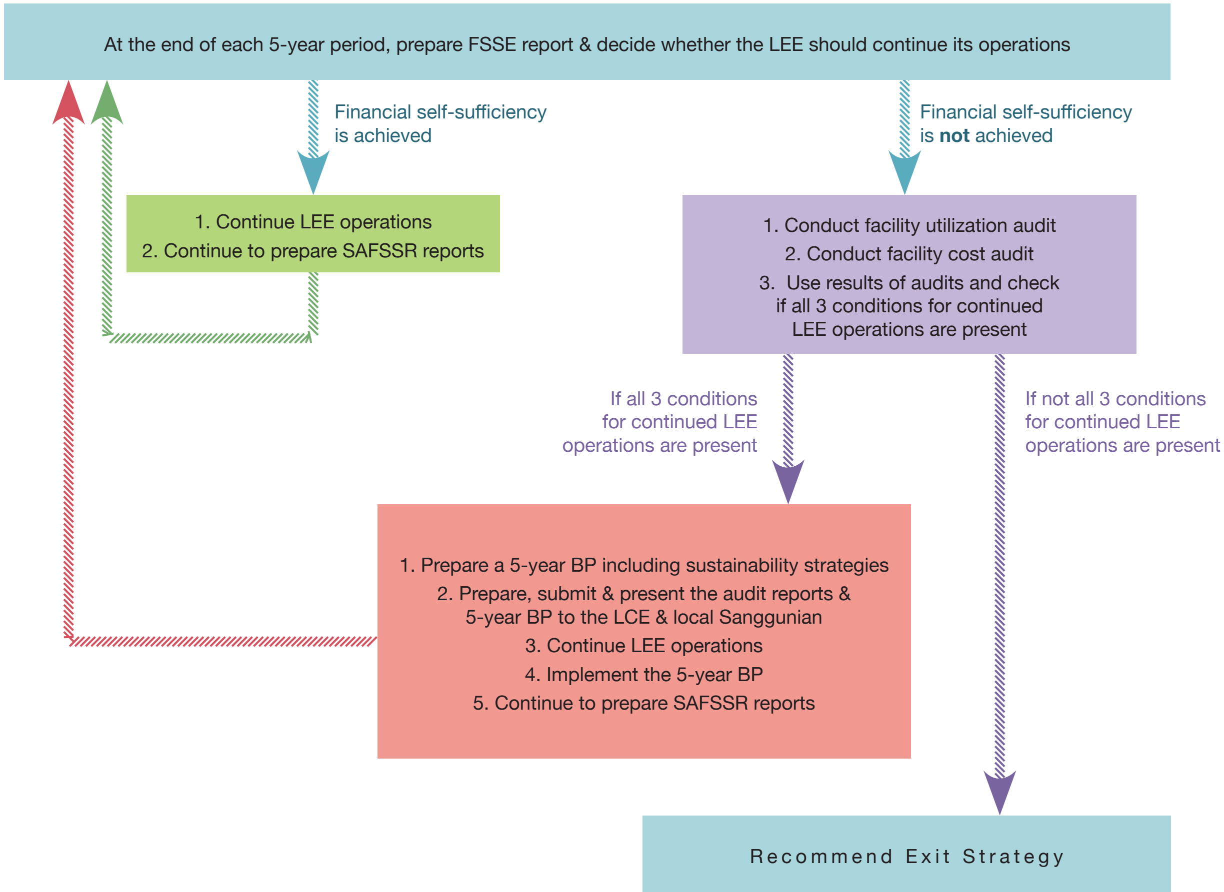
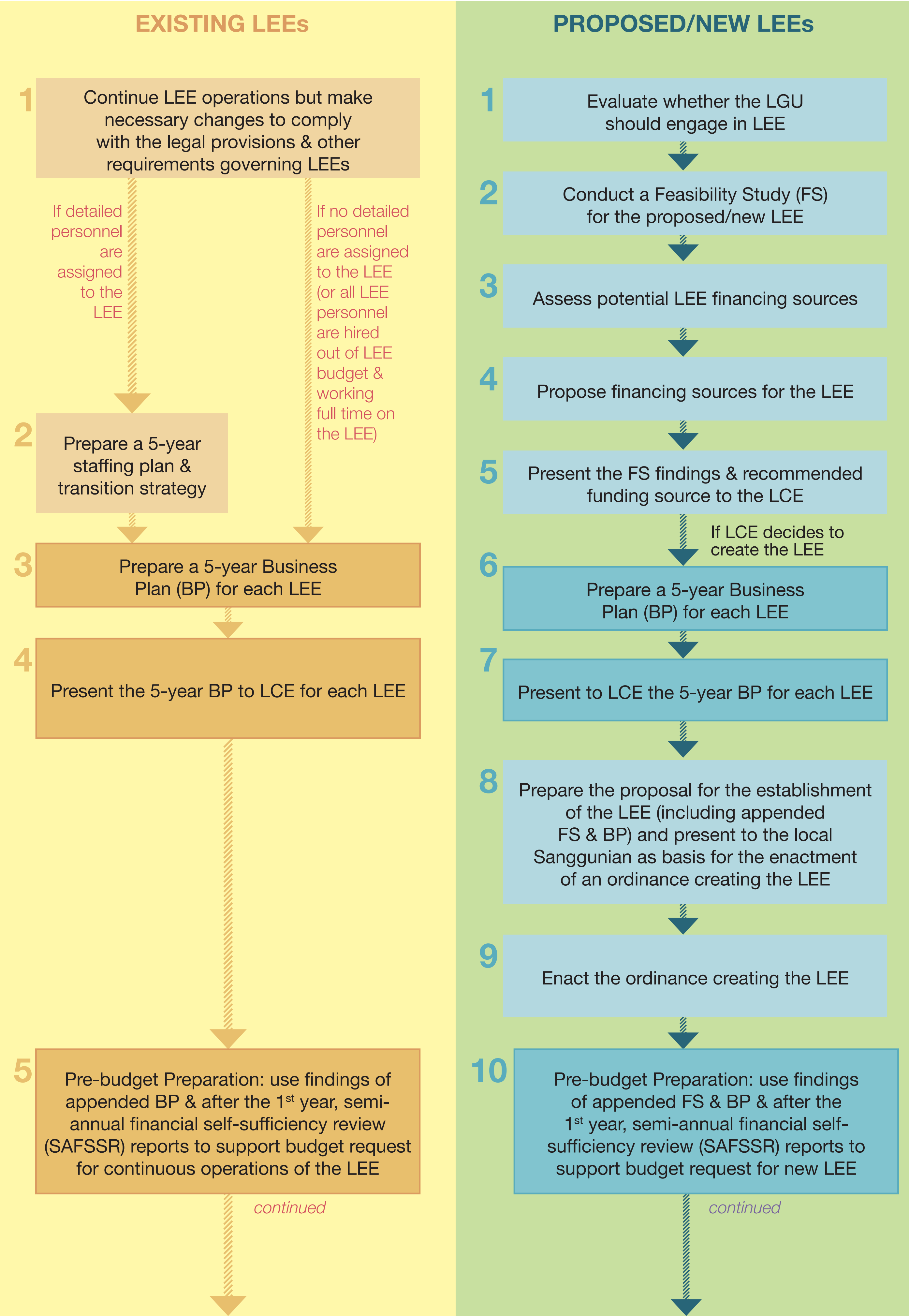


Figure 7. Overall Process Flow Diagram for Existing and Proposed/New LEEs



EXISTING LEEs

from previous

6

Budget Preparation:

1. Include in the budget call of the general fund annual budget the specific guidelines for preparation of LEE AOB
2. Prepare & submit LEE AOB
3. Conduct budget hearing & evaluate LEE AOB proposal
4. Include the LEE AOB in the LEP that will be submitted to the LCE for approval
5. Provide inputs pertinent to the LEE AOB for the budget message
6. Submit the LEE AOB to the local Sanggunian

7

Budget Authorization:

1. Enact the appropriation ordinance
2. Approve the appropriation ordinance for LEE
3. Submit the appropriation ordinance review

8

Budget Review:

1. Check the appropriation ordinance with the appended budget documents
2. Review the appropriation ordinance
3. Issue the review action

9

Budget Execution:

1. Record the approved appropriation in LEE's books of accounts
2. Prepare cash & summary of financial & physical performance targets using prescribed forms in the BOM
3. Obligate and disburse funds
4. Adjust cash program for shortages & overages
5. Provide corrective measures for negative deviations

continued

PROPOSED/NEW LEEs

from previous

11

Budget Preparation:

1. Include in the budget call of the general fund annual budget the specific guidelines for preparation of LEE AOB
2. Prepare & submit LEE AOB
3. Conduct budget hearing & evaluate LEE AOB proposal
4. Include the LEE AOB in the LEP that will be submitted to the LCE for approval
5. Provide inputs pertinent to the LEE AOB for the budget message
6. Submit the LEE AOB to the local Sanggunian

12

Budget Authorization:

1. Enact the appropriation ordinance
2. Approve the appropriation ordinance for LEE
3. Submit the appropriation ordinance review

13

Budget Review:

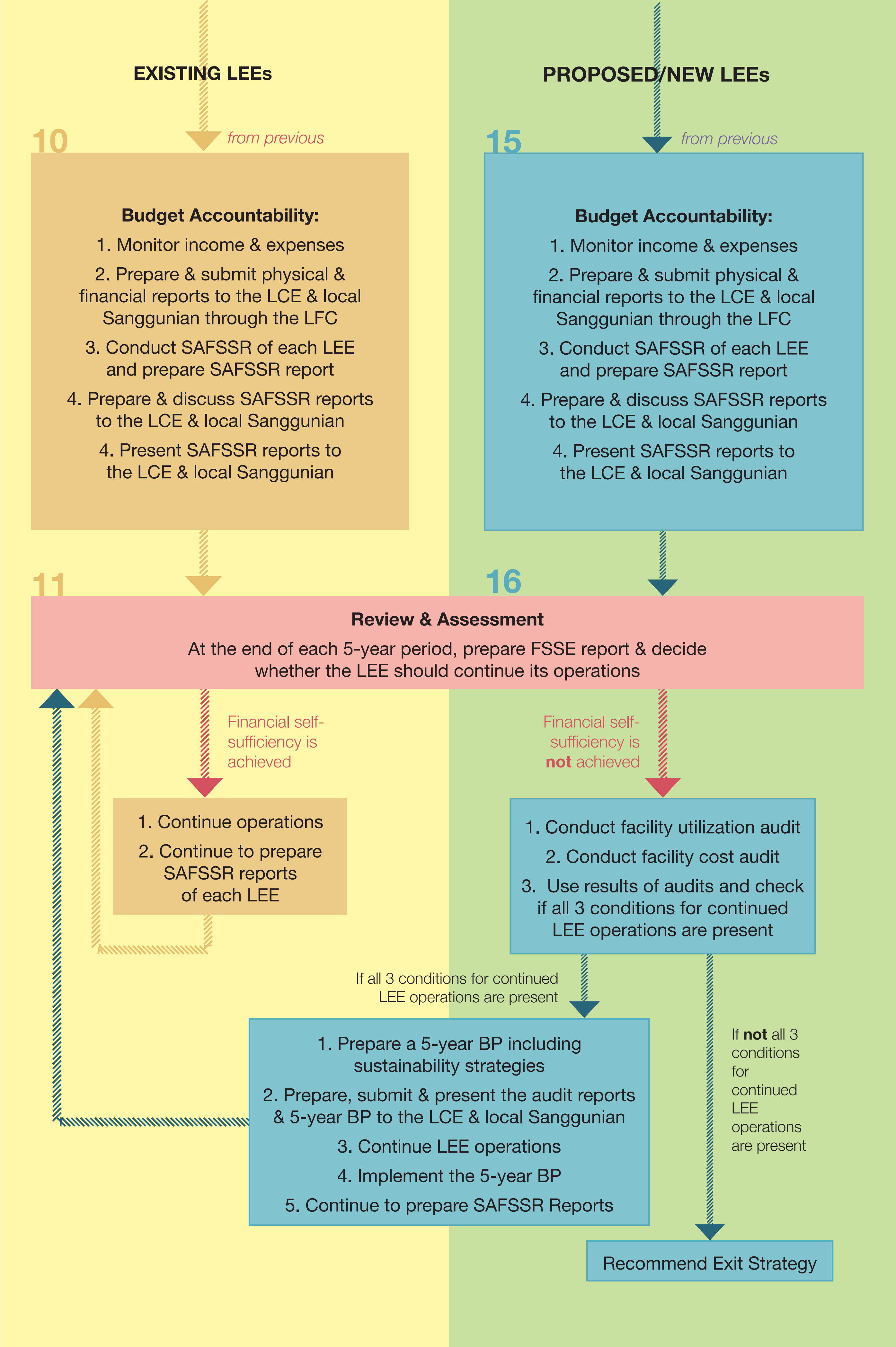
1. Check the appropriation ordinance with the appended budget documents
2. Review the appropriation ordinance
3. Issue the review action

14

Budget Execution:

1. Record the approved appropriation in LEE's books of accounts
2. Prepare cash & summary of financial & physical performance targets using prescribed forms in the BOM
3. Obligate and disburse funds
4. Adjust cash program for shortages & overages
5. Provide corrective measures for negative deviations

continued


EXISTING LEEs
PROPOSED/NEW LEEs
10
from previous
Budget Accountability:
1. Monitor income & expenses
2. Prepare & submit physical & financial reports to the LCE & local Sanggunian through the LFC
3. Conduct SAFSSR of each LEE and prepare SAFSSR report
4. Prepare & discuss SAFSSR reports to the LCE & local Sanggunian
4. Present SAFSSR reports to the LCE & local Sanggunian
15
from previous
Budget Accountability:
1. Monitor income & expenses
2. Prepare & submit physical & financial reports to the LCE & local Sanggunian through the LFC
3. Conduct SAFSSR of each LEE and prepare SAFSSR report
4. Prepare & discuss SAFSSR reports to the LCE & local Sanggunian
4. Present SAFSSR reports to the LCE & local Sanggunian
11
16
Review & Assessment
At the end of each 5-year period, prepare FSSE report & decide whether the LEE should continue its operations
Financial self-sufficiency is achieved
1. Continue operations
2. Continue to prepare SAFSSR reports of each LEE
Financial self-sufficiency is not achieved
1. Conduct facility utilization audit
2. Conduct facility cost audit
3. Use results of audits and check if all 3 conditions for continued LEE operations are present
If all 3 conditions for continued LEE operations are present
1. Prepare a 5-year BP including sustainability strategies
2. Prepare, submit & present the audit reports & 5-year BP to the LCE & local Sanggunian
3. Continue LEE operations
4. Implement the 5-year BP
5. Continue to prepare SAFSSR Reports
If not all 3 conditions for continued LEE operations are present
Recommend Exit Strategy

8. AN "EFFECTIVE" LEE IS ACHIEVABLE: BEST PRACTICES

An effective LEE – "one that contributes to the quality service delivery goals of the LGU" – is achievable under the existing policy framework. An effective LEE can be realized if it is designed, set up, operated, and managed in accordance with a well-prepared FS and a detailed BP as envisioned in this LEE manual.

Discussed below are cases of two LEEs which indicate that LEEs can contribute to the quality service goals of the LGU and at the same time achieve financial self-sufficiency.

8.1 Benguet General Hospital (BeGH)

The case of the Benguet General Hospital (BeGH) shows that if the guidelines set out in this LEE Manual were meaningfully applied, even the provision of so-called social services can be done via a LEE mode.

The physical transformation of BeGH was in response to a problem jointly perceived by the LGU constituents and political leadership – that BeGH could scarcely answer the needs of the people of Benguet and other neighboring communities because the medical equipment and services of the hospital were adjudged as severely inadequate.

In response, the provincial government formally requested and was granted by the Japanese government through the Japan International Cooperation Agency (JICA) a Php 842 million health care upgrading grant for BeGH. A new 200-bed BeGH complex was turned over to the LGU in April 2000.

The grant solved the facility upgrading problem of BeGH. However, the equally critical problem of meeting the larger operational requirements of the expanded physical facility remained. The two major operational problems were:

1. Meeting the need for additional personnel without the province exceeding the PS cap; and
2. Providing for additional funds to meet maintenance and other operating requirements.

To resolve these operational problems, the then provincial governor proposed in August 2000 to operate the hospital as an LEE based on the findings of a project study report conducted by a duly organized BeGH task force.

The governor and the task force cited the following advantages of operating BeGH as an LEE:

1. The province will be able to create and hire additional personnel to beef up the personnel requirements of the hospital without violating the restrictions fixed under Section 325 of the LGC;
2. Income generated from the operations of the hospital will be treated as trust funds to be plowed back solely for the operations of the hospital, thereby promoting self-sustenance and proper maintenance of its facilities and equipment;
3. There will be fiscal autonomy which will reduce bureaucratic hassle which hinders the expeditious acquisition of critical medicines and hospital requirements necessary for hospital operations; and
4. It will provide sufficient flexibility to the province in the structuring of its personnel staff for the efficient and economical management of its operations.

In CY 2004 (four years after the proposal was submitted to the Sanggunian Panlalawigan), the province, under Provincial Ordinance No. 04-90, series of 2004, declared the said new hospital complex as an economic enterprise.

The ordinance creating the LEE also laid down the following:

1. The terms of reference for the management and operation of the hospital created a Board of Directors to oversee the issuance of policies and guidelines governing the day-to-day management and operations of the hospital as an economic enterprise; and
2. A declared annual subsidy of Php 40,000,000 with additional allocation if needed to start the operations of the upgraded hospital with the condition that the subsidy ceases when the hospital becomes financially viable.

In 2007, to set the path towards long-term sustainability for BeGH, a business development plan covering the period 2007-2016 was prepared. The business development plan charted a path seeking to maintain the delicate balance between providing access to quality medical services to all the LGU constituents, particularly the poor, and generating revenues sufficient to sustain its operating requirements.

The business development plan provided for a system of cross subsidy wherein revenues from the operations of its pharmacy and diagnostics services, the use of its private rooms, operating rooms, and special units subsidized the cost of providing free services to indigent patients.

Guided by this business development plan, BeGH has been able to reduce its dependence on LGU subsidy despite increases in operating costs as shown in Table 1.

Table 1. Benguet General Hospital: Operating Budget and LGU Subsidy, 2007-2016

Year	Operating Budget In Php '000 (1)	Annual LGU Subsidy In Php '000 (2)	LGU Subsidy as % of Operating Budget % (3)=(2)/(1)
2007	91,148	40,000	43.9%
2008	96,147	40,000	41.6%
2009	103,058	40,000	38.8%
2010	117,552	40,000	34.0%
2011	123,348	40,000	32.4%
2012	129,848	40,000	30.8%
2013	139,815	37,000	26.5%
2014	148,457	35,000	23.6%
2015	158,501	35,000	22.1%
2016	172,832	25,000	14.5%
Annual Growth Rate	**7.4%**	**-5.1%**	

Source of Basic Data: BeGH

Despite operating costs increasing on the average by 7.4% annually (from Php 91 million in 2007 to an estimated Php 173 million in 2016), the subsidy received by BeGH from the provincial government declined annually by 5.1% from Php 40 million in 2007 to an estimated Php 25 million in 2016. Thus, the dependence of BeGH on LGU subsidy declined from 44 % in 2007 to only 14% by 2016. This clearly shows that BeGH was proceeding towards financial self-sufficiency despite rising operating costs.

The contributing success factors were identified as follows:

1. Good governance
    a. Strong leadership/political will and support from local officials, the LCE, the management committee, and the hospital board;
    b. Prompt amendment/updating of the provincial revenue code as basis for the collection of hospital fees;
    c. Active partnership with the private sector; and
    d. Compliance with accounting, auditing rules and regulations, and the Procurement Law.
2. Delivery of quality health services (physical and human infrastructure)
    a. Utilization of income to improve and upgrade equipment and hiring of additional personnel (casual, contract of services) to augment existing personnel in accordance with the staffing pattern;

   b. Outsourcing of services (e.g., dialysis and 2-D echo);
   c. Procurement and upgrading of hospital, medical, dental and laboratory equipment, and
   d. Maintenance of facilities and equipment.

3. Regulation
   a. Compliance to Department of Health (DOH) standards for license to operate;
   b. Compliance to Philippine Health Insurance Corporation (PHIC) standards for accreditation; and
   c. Compliance to other standards of other regulatory bodies.

4. Health care financing
   a. Enrolment of indigent patients with the PHIC (sponsored);
   b. Point-of-care system;
   c. Financial assistance from partners; and
   d. Hospital income utilization.

5. Health systems development
   a. Strengthening of health information systems and installation of the hospital computerization system;
   b. Internal/external audit;
   c. Monitoring; and
   d. Strengthened referral system for indigent patients.

6. Health human resources
   a. Training of personnel/capability building;
   b. Commitment/dedication of management and hospital personnel; and
   c. Visiting consultants (various specialties).

In 2016, the BeGH prepared a new plan that aimed to further improve its service quality as well as its revenue-generating capacity. The new plan covered the following:

1. Upgrading of the hospital level;
2. Expansion of private rooms and intensive care units;
3. Procurement of appropriate equipment;
4. Implementation of the residency training program;
5. Establishment of rehabilitation clinics; and
6. Full implementation of electronic information system (BizBox to include Hospital Materials Management and Inventory Systems or HOMIS).

Thus, BeGH embarked on a new and higher cycle of planning-investment programming-budgeting for the LEE.

8.2 Ormoc City Waterworks and Sewerage Authority

The Ormoc City Waterworks and Sewerage Authority (ORWASA) was established in 1960 by the National Waterworks and Sewerage Authority (NAWASA) as a water service provider for the city of Ormoc. During the mid-1970s, the facilities of ORWASA were turned over to the city government. Since then, the city government has been operating the ORWASA as an LEE.

The LGU was justified in operating ORWASA as an LEE since it satisfied all four hurdle criteria for an LGU operating an LEE as set out in this manual:

1. ORWASA satisfied a basic development need of the LGU — water supply (Criteria 1);
2. There was no other water service provider serving the city (Criteria 2);
3. ORWASA can be operated as a business enterprise (Criteria 3); and
4. ORWASA can be operated with technically capable personnel (Criteria 4).

ORWASA was a public utility (PU) that was able to fully finance its operating requirements from income derived from its operations. Based on the 2014 Statement of Income and Expenses provided by ORWASA, the LEE generated total income of Php 33.6 million and incurred operating expenses of Php 26.8 million, recording a net income of Php 6.8 million.

Despite its net income, however, ORWASA recognized the need to further improve its financial performance. With its plant and operating assets (net of depreciation) declared in its 2014 Balance Sheet valued at Php 392.0 million, ORWASA earned a rate of return on its fixed asset base of 2.12%, way below the 12% ceiling allowed for public utilities. The rate of return on the Php 474.7 million LGU equity was only 1.8%.

In 2016, ORWASA's management drew up a plan to improve the LEE's financial performance by increasing revenues through:

1. Improved billing and collection; and
2. Increases in water rates from the current comparatively low rate of Php 4.00 per cubic meter. ORWASA's water rate was just one-fifth of the average water rate of Philippine water districts of Php 19.56 per minimum consumption of 10 cubic meters.

Table 2. ORWASA Income and Expenditures FYs 2011-2015

ORWASA TOTAL INCOME AND EXPENDITURES FYs 2011-2015					
	2011	**2012**	**2013**	**2014**	**2015**
TOTAL INCOME	34,367,973.22	45,843,901.95	27,505,838.96	33,584,352.33	37,320,684.51
TOTAL EXPENDITURES	39,246,196.86	49,905,722.47	35,581,238.43	26,783,832.76	33,908,449.15
NET INCOME	(4,878,223.64)	(4,061,820.52)	(8,075,399.47)	6,800,519.57	3,412,235.36

* ORWASA received transfers from the General Fund only in FYs 2011 and 2012

** Expenditures for FYs 2011, 2012, 2013 and 2015 included Capital Outlays

Appendix

APPENDIX A. BUSINESS PLAN OUTLINE[13]

I. Cover Sheet

Use a cover sheet if the LGU is trying to attract investors or planning to avail of bank financing.

A. LEE Information

1. Full official name of LEE as stated in the appropriation ordinance
2. Complete address of the LEE
3. Main contact person and his/her designation
4. Contact numbers

B. Brief paragraph describing the LEE goals, potentials, and outlook

C. Amount of capital required by the LEE for its current and future needs

II. Table of Contents

III. Executive Summary

This summary encapsulates the Business Plan in a few paragraphs, preferably between two and five pages. The summary must be able to capture the interest of the reader as well as demonstrate that the LGU knows what it wants for the LEE, and where it is headed.

IV. Profile of the LGU

A. Brief background on the LGU – location, economic base, role in province or region, vision, development trends, and direction

B. List of key elected and appointive officials

V. Product or Service Description

A. Brief history of the LEE

B. Reason for starting or expanding the LEE

C. Legal basis and related ordinances for the LEE

D. Goals and objectives of the LEE

E. Description of the LEE's product or service

F. How the product is made or service provided

G. How the product or service of LEE differs from similar products or services or LEEs

13 Adapted from Covello, Joseph A and Hazelgren, Brian J., The Complete Book of Business Plans (Illinois: 2006).

VI. Market Analysis

A. Description of the existing marketplace or industry (to which the product or service or LEE belongs) including trends

B. Economic forecasts that indicate spending/consumption trends favorable to the industry and the LEE

C. Profile of the target customers in terms of:

1. Demographics – age, income, etc.
2. Lifestyle of target customers – attitudes, preferences, habits
3. Geographical location

D. Description of competition

1. Who are the competitors
2. Description of competitors' product or service features
3. How the competitors promote their products or services

E. Distinct advantages and disadvantages of the LEE's product or service versus its competition in the following areas:

1. Actual performance
2. Quality and reliability
3. Distribution
4. Pricing
5. Public image or reputation

VII. Marketing and Sales Strategy

A. Market analysis - Put yourself in the customer's place and ask: a) " Where do I go to buy it?"; b) "What makes me buy it?"; c) "What media do I watch, read, and listen to that makes me decide to buy the product or service or patronize the LEE?"

B. Pricing strategy (How price is set?) - Remember to charge what the market will bear. Do not over- or underprice your product or service.

C. Marketing budget – A general rule of thumb: allocate 5 to 10% of expected annual revenues to marketing expenses.

D. Timetable to market the product or service

E. Professional services needed to implement the Marketing Plan

F. How the product or service will be marketed and advertised – publicity and promotion, including:

1. Promotional giveaways (t-shirts, hats, pens, mugs, fans, etc.) showing logo and brand name
2. Advertising over local radio station, local newspaper
3. Press releases

4. References to the LEE during public speeches, meetings, conventions attended by LGU officials and staff

5. Posters, billboards in strategic locations

G. Marketing objectives – can be expressed in terms of increasing revenues by a certain percentage over a certain time frame.

VIII. Management and Personnel Plan

A. Formal organizational structure including names of members of management team and their corresponding job descriptions

B. Strengths of the management team, e.g., qualifications and experience managing the sales, marketing, finance, and operations units

C. External human resources – e.g., consultants, lawyer, etc.

D. Personnel Plan – personnel required to support operations and the intended growth of the LEE

IX. Financial Projections

Monthly projections for first and second years of operations; annual projections thereafter for third to tenth year.

A. Important assumptions

B. Selling, general, and administrative expenses

C. Revenue forecasts

D. Breakeven analysis

E. Projected profit and loss

F. Projected cash flow

G. Projected balance sheet

H. Financial ratios

1. Profitability ratios – Gross Margin, Profitability Margin, Return on Assets, Return on Equity

2. Liquidity ratios – Current Ratio, Quick Ratio, Net Working Capital, Interest Coverage

3. Debt ratios – Debt-to-Net Worth, Short Term Liabilities to Liabilities

4. Activity ratios – Accounts Receivable Turnover, Collection Days, Inventory Turnover, Accounts Payable Turnover, Total Asset Turnover

5. Other ratios – Assets to Sales, Debt to Assets, Current Debt to Total Assets, Acid Test, Asset Turnover

APPENDIX B. DOCUMENTARY REQUIREMENTS FOR BUDGET REVIEW

1. Proposed New LEE

1.1. LCE-approved feasibility study report submitted to the local Sanggunian;

1.2. LCE-approved business plan submitted to the local Sanggunian; and

1.3. Certification from the LGU budget officer that the full amount of the LEE project cost is included in the duly approved current year AIP.

2. Existing LEEs

2.1. LCE-approved business plan submitted to the local Sanggunian

2.2. After the first year, SAFSSR reports

2.3. Actual LEE income statement for the past three (3) years and the projected income statement for the coming budget year.

2.4. If the LEE fails to cover 100% of the operating requirements of the LEE by the end of the 5th year, then the LGU must submit the following reports:

2.4.1. Facility utilization audit report findings providing the following information:

a. Current year gross revenue vs. full capacity revenue; and

b. Proposed measures to increase gross revenues of full capacity.

2.4.2. Facility cost audit report findings providing the following information:

a. Actual cost of operating the LEE including financial cost vs. "true" full cost of running the LEE. Annual operating and financial costs shall be broken down as follows:

1. Direct costs like direct material cost, labor, and utility costs;
2. Management costs;
3. Other overhead costs;
4. Capital costs exclusive to the operation of the LEE; and
5. Joint capital and related operating costs that it shares with the rest of the LGU organization like shared offices, computers, and telecommunication facilities.

b. If actual total cost is either lower or higher than the true total cost, cost items that contributed to the variance shall be identified with their respective contributions and the reasons for the variances.

c. Proposed measures to reduce the variance.

APPENDIX C. FORMAT FOR SEMI-ANNUAL FINANCIAL SELF-SUFFICIENCY REVIEW (SAFSSR) REPORT

SEMI-ANNUAL FINANCIAL SELF-SUFFICIENCY REVIEW (SAFSSR) REPORT

Name of LEE:____

For the Semi-Annual Period Covering: ____________________________

Item	Amount (Php)
A. Total Income	
B. Expenses	
B.1. Personnel Services	
B.2. MOOE	
B.3. Finance Charges - Interest Expense	
Total Expenses	
C. Net Income (Loss)	
D. % Financial Self-Sufficiency (Tot Income / Tot Expenses x 100)	

Analysis:

Prepared by: **Noted by:**

APPENDIX D. FORMAT FOR FINANCIAL SELF-SUFFICIENCY EVALUATION (FSSE) REPORT

FINANCIAL SELF SUFFICIENCY EVALUATION (FSSE) REPORT

Name of LEE:____

For the 5-Year Period Covering: ________________________________

Item	Year 1: 2016		Year 2: 2017		Year 3: 2018		Year 4: 2019		Year 5: 2020		5-Year Cumulative Total
	Jan-June	Jul-Dec	Jan-June	Jul-Dec	Jan-June	Jul-Dec	Jan-June	Jul-Dec	Jan-June	Jul-Dec	
A. Total Income											
B. Expenses											
B.1. Personnel Services											
B.2. MOOE											
B.3. Finance Charges - Interest Expense											
Total Expenses											
C. Net Income (Loss)											
D. % Financial Self Sufficiency (Tot Income / Tot Expenses x 100)											

Analysis :

Recommendations:

Prepared by: **Noted by:**

APPENDIX E. CONDUCTING A FACILITY UTILIZATION AUDIT FOR A LEE

The facility use audit for LEEs needs to consider four (4) basic aspects of good or service delivery that LEEs shall consider.

1. **Technical Aspects** – These include:
    a. Coverage and Service Levels - proportion of LGU population and in what areas of the LGU, by type of service;
    b. Delivery Performance - is the provision of good or service reliable, catering to actual demands, of sufficient quality, and LEE facilities appropriately operated and maintained; and
    c. Investment Planning - how well does the LGU plan for future investments necessary for the expansion and improvement of the LEE service level.
2. **Financial Aspects** – service pricing including cost recovery through tariffs, and affordability and willingness to pay, sources of revenue, payment collection, and debt servicing.
3. **Organizational Issues** – organizational issues, which affect the LEE's day-to-day operations like operating structure, human resources, and capacity issues.
4. **Community Aspects** – social and cultural issues and community education affecting the LEE facility operations.

These four components of the facility utilization study are interrelated and the required studies shall be undertaken as a package.

A multi-disciplinary technical team of the LGU composed of an economist, an engineer, an accountant/financial analyst, a statistician/data analyst, and a management analyst can do the studies. Whenever necessary, outside technical consultants may be engaged by the LGU to provide specialized technical inputs/advice to the study team.

I. Technical Studies

A. Coverage and service levels
    i. Coverage is the share in percentage terms of the LGU population that is actually served by the LEE.
    ii. Service levels refer to the quality of the LEE-provided good or service received.
    iii. This study component needs to establish the following:
        1. What are the technical methods for delivering the LEE-provided good or service?
        2. What percentage of the population has access to the good or service? In other words, what is the level of coverage?
        3. What are the service levels for different types of users?
        4. What are the social, environmental, and/or economic costs of any shortcomings in coverage or service levels?
    iv. Assessment approach - Using secondary sources, key informant interviews, and field visits, the study team can gain a basic understanding of the technical nature of the system, the share of the population that receives services, the quality of those services, and the effects of shortcomings on residents, businesses, and the natural environment.

B. Delivery Performance

i. This study component needs to establish the following:

1. What is the condition of the physical assets used to deliver the LEE-provided good or service?
2. What maintenance activities are undertaken for the LEE facilities?
3. What is the level of LEE facility "revenue leakages", and the factors behind such leakages or foregone revenues?

ii. Assessment Approach

1. Use secondary sources and interviews to approximately establish the physical condition of the LEE's productive assets.
   a. Determine whether the overall system is in good, fair, poor, or very poor condition.
   b. Then put particular attention on any parts of the system that are in poor or very poor condition, such as leaking roofs, clogged toilets, busted water lines, etc.
2. Use expenditure records and programs of work as well as interviews to identify and evaluate the maintenance programs in place for the LEE facilities.
3. Calculate estimates of revenue leakages by comparing actual revenues from LEE financial statements with potentially collectible revenues based on design capacities. Supplement results from secondary data with field observations, surveillance and interviews.

iii. Investment Planning

Capital investment is one standard way to address technical deficiencies in LEE service systems. When service levels or coverage are too low, LEEs can upgrade facilities to improve services or extend their coverage areas to previously unserved neighborhoods in the LGU.

i. This study component needs to establish the following:

1. What types of capital investments are needed to improve LEE service coverage and/or service levels?
2. What types of capital investments are needed to reduce revenue leakages?

ii. Assessment Approach

1. Develop a list of the service level and coverage deficiencies using the assessment carried out in the Coverage and Service Levels assessment.
2. Develop a list of factors contributing to major technical losses in the system using the assessment carried out under the Delivery Performance assessment.
3. For each noted deficiency, identify the necessary capital investments.

II. Financial Studies

A. Service Pricing

The pricing of LEE-provided goods and services requires the simultaneous achievement of three often-contradictory objectives: financial sustainability of the LEE, affordability to customers, and equity in the allocation of costs to end-users. The underlying principle is "user pays." But its implementation will vary from place to place and type of good/service, depending on the ability and willingness to pay of customers and the LGU commitment to sound financial management.

i. This component needs to establish the following:

1. Are LEE-provided goods or services delivered on a cost recovery basis? That is, do the LEE revenues cover or exceed expenditures?
2. Are LEE-provided goods or services affordable to customers, and are customers "willing to pay" for such goods and services?
3. Does the LEE pricing structure equitably allocate costs to customers?

ii. Assessment Approach

1. Financial sustainability of LEE

Financial Sustainability: Methodology, Data Needs and Data Sources

Methodology	Data Needs	Data Sources
Consult existing secondary sources, LEE staff, and local key informants to gain a qualitative and, where possible, quantitative understanding of the extent to which revenues cover costs. Look at the last three years to get a sense of trends over time. a. Do total revenues cover total costs? What is the order of magnitude of the surplus or (deficit)? b. Do revenues from user charges cover operating costs? Or capital investment? c. Do total revenues cover operating costs? To what extent does the LGU or other entity (e.g., higher LGU level, national government, private organizations) subsidize O&M or capital investment?	• Operating cost • Capital investment costs • Revenues from user fees • Revenues from other sources	• Existing reports • Key informant interviews with manager and staff of the LEE, LGU officials, local civil society organizations (CSO) experts

2. Affordability and Willingness to Pay (WTP) Assessment

Affordability and Willingness to Pay (WTP): Methodology, Data Needs and Data Sources

Methodology	Data Needs	Data Sources
Consult existing secondary sources, LEE staff, and local key informants to gain a qualitative and, where possible, quantitative understanding of the extent to which the LEE-provided goods or services are affordable to customers/end users. a. Consider residential users first, and then other users, such as commercial firms and industrial companies. b. For residential users, review existing comparisons of user charges to household income. • What percentage of household income is spent on the LEE-provided goods or services? • How does this percentage vary by income level? • In particular, what percentage of income do poor and very poor households spend on the LEE-provided goods or services? c. Look at any changes in prices or household incomes in the past three years to get a sense of the trend over time. Conduct a “willingness to pay” assessment on existing and potential LEE customers to assess the type of LEE products or services most desired by the target users and the amount they are willing to pay for the desired product or service features.	• Household income by population segment (e.g., by income class) • Household expenditure data, including expenditures on the expenditure type to which the LEE-provided good or service belongs. • Existing LEE pricing structure • WTP of existing and potential LEE customers	• Existing reports on household income and expenditures or affordability studies • Key informant interviews with accounting staff of LEE, LGU officials, CSOs, local key informants • WTP survey for LEE-provided goods or services

3. Equity

Equity: Methodology, Data Needs, and Data Sources

Methodology	Data Needs	Data Sources
Consult existing secondary sources, LEE staff, and local key informants to ascertain the pricing structure and the way it allocates costs among customers. This issue has a number of different aspects: **Allocation of costs among user groups** – Are industrial and institutional users charged different rates than residential users? What is the rationale for this? Is it fair for households to pay less for a given unit of service delivered than say, a commercial establishment? **Pricing by level of good or service consumption** – Do prices vary by level of consumption? Do customers that consume less pay less for the first few units consumed? [Rationale: to increase affordability for low-income groups.] Or do customers that consume large amounts pay less for unit? [Rationale: quantity discount for large industrial and other users.] Are these pricing policies equitable? **Charges to new users vs. charges to existing users** – How are the costs of service expansion distributed among different users? Do customers in new service areas pay the same amount as customers in existing neighborhoods? Do new customers pay an upfront fee (e.g., connection charge) to cover part of the cost of building the network extension?	• Domestic user tariff • Industrial user tariff • Institutional and other user tariff • Unit charges by ranges of quantity consumed for different types of users • Connection or access fees for LEE services • Other user charges	• LEE accounting office • Existing reports on LEE pricing • Key informant interviews with LGU officials, CSOs, local key informants

4. LEE Financing Sources

A key financing challenge facing many LEEs in the Philippines is mobilizing sufficient funding to provide adequate services. Financing issues include:

i. Funding is always needed for proper LEE O&M.

ii. Where systems are in poor condition or the population of the service area is growing quickly, substantial funding is also needed for facility improvements and expansion.

iii. Most LEEs do not make adequate use of user charges, because they do not know how much they can change or "unwillingness to charge" because LGU officials have not mustered the political will and public support necessary to raise prices.

iv. Many LEEs have not yet been able to tap credit and debt markets in order to pay for capital improvements gradually over time.

v. Traditionally, LEEs have been overly dependent on subsidy transfers from city/municipal, provincial, or national budgets.

Meeting the financing challenge requires LEEs to mobilize a broader range of financing sources for operations and capital investment.

i. This component needs to establish the following:

1. What sources of finance are currently being used to cover the cost of LEE good or service provision?
2. What additional financing sources could the LEE mobilize to pay its debts, including advances from the LGU general fund or improve/expand its facilities?

ii. Assessment approach

1. Existing sources of LEE finance

Existing Sources of LEE Finance: Methodology, Data Needs, and Data Sources

Methodology	Data Needs	Data Sources
Consult existing secondary sources, LEE staff, and local experts to gain a qualitative understanding of the sources of finance for service delivery • Consider separately: (a) O&M and (b) capital investment • Identify sources of financing for operation and maintenance, including user charges and subsidies from local governments • Identify sources of financing for capital investment, including bank loans, bonds, LGU capital contributions, and private investors	• Sources of finance for O&M • Source of finance for capital investment	• Existing reports • Key informant interviews with manager and senior finance staff of LEE, LGU officials, CSOs, local key informants

2. Additional Sources of LEE Finance

Additional Sources of LEE Finance: Methodology, Data Needs, and Data Sources

Methodology	Data Needs	Data Sources
Consult with LEE management, LGU officials, and/or local finance experts to gain a qualitative understanding of the potential for expanding the existing sources of finance to include: • Bank loans • LGU bonds • Private investment • Other non-traditional instruments for LEE financing Key elements of the feasibility of introducing such methods include: • Local political support • LGU capacity to tap the credit market or to enter into PPP arrangements • Creditworthiness of the LEE and/or the LGU • Risk appetite of potential PPP investors	• Features of government bank lending to LGUs in the Philippines • Features of LGU bond issues in the Philippines • Possibilities for private investment in LEEs via PPP in LEEs in the Philippines	• Existing reports • Key informant interviews with manager of LEE, LGU officials, bankers, private providers of municipal services, local finance experts

3. LEE Collection Performance and Debt Service

Many customers of LEEs are reluctant to pay their bill in full and on time. They either feel that the cost of service shall be covered by the LGU or, more often, that the quality of service that they receive does not merit the charges levied on their bill. Improving the payment collection rate — that is, the ratio of tariff payments collected from customers to tariff payments charged to customers — therefore requires improving public perception of the LEE and the good or service they deliver. When LEE charges are affordable and customers feel that they are getting "value for money," they will pay their bills.

i. This component needs to establish the following:

1. To what extent are current LEE charges being collected from customers?
2. Do LEE customers have substantial debts from previous weeks, months, and even years? How does this affect accounts payable of the LEE?
3. To what extent does the LEE facilitate payment by customers?

ii. Assessment Approach

1. LEE Collection Efficiency

LEE Collection Efficiency: Methodology, Data Needs, and Data Sources

Methodology	Data Needs	Data Sources
Are payments for LEE-provided goods or services collected by the LEE, the LGU, banks, payment centers, or other entities? Determine the collection efficiency of the LEE. This is the ratio of customer payments received to (current) collectibles for the LEE-provided goods or services. Where payments received by the LEE are significantly less than charges levied by the LEE, establish the causes for the payment arrears.	• Institutional arrangements for collecting tariff payments • Ratio of user payments to user charges by type of user group	• Existing reports • Key informant interviews with LEE manager, LGU officials, and LEE billing and collection staff

2. LEE Receivables from Customers

LEE Receivables from Customers: Methodology, Data Needs, and Data Sources

Methodology	Data Needs
Determine the total amount of receivables from LEE customers Compare it to annual LEE revenues to get an idea on the order of magnitude	• Total amount of receivables from LEE customers • Total LEE annual revenues

3. LEE Collection System

LEE Collection System: Methodology, Data Needs, and Data Sources

Methodology	Data Needs	Data Sources Data
Analyze the modalities for payment by LEE customers and evaluate qualitatively how easy it is for customers to pay. Does the LEE billing and collection system have a customer follow-up system to remind customers when payments are due and follow up on delinquent customers? What measures are taken in case of non-payment, e.g., denial of service?	• Payment modalities available to customers • Customer payment follow-up system	• Billing and collection section of LEE

III. Organizational Studies

The assessment of the quality of the organization of an LEE needs to look into two key components:

- Organizational structure; and
- Human resources.

The organizational structure of LEEs can affect how well they are able to provide services, manage day-to-day operations, and carry out facility planning. Having an effective organization can help resolve LEE good or service delivery problems and interruptions when they arise, increase levels of good or service provision, and generally improve the quality of LEE good or service provision for its customers.

In addition, service providers shall periodically evaluate their performance against formal targets. Only by setting these goals, and measuring actual performance against them, can LGUs determine how effectively their LEEs are operating.

Finally, LEE shall be guided by a business plan that provides guidance to the LEE both for regular operations and for longer-term investments.

The managerial and technical capacity that the LEE has directly affects its ability to deliver goods or services to its customers.

a. Organizational aspects

   i. This component need to establish the following:

      1. Is the LEE organized effectively?

      2. How effectively is the LEE conducting performance monitoring and strategic planning?

ii. Assessment approach

1. Effectiveness of LEE Organization

Effectiveness of LEE Organization: Methodology, Data Needs, and Data Sources

Methodology	Data Needs	Data Sources
Assess the organizational arrangements of the LEE. The key aspects to look into include: • Does the LEE have a clear management structure or organization chart, which shows who reports to whom? • Are lines of responsibility well documented and transparent? • Do the various parts of the organization communicate with each other effectively? • Do employees understand their daily or primary duties and are they sufficiently monitored in their activities? • Are LEE management and employees held accountable if quality standards are not met?	• Organizational chart of LEE • Set operating systems and procedures for organizational coordination • Actual organizational coordination practices • Staffing pattern	• Interviews with LEE management and staff • Existing manuals, systems, and procedures • Existing internal and external reports

2. Performance Monitoring and Strategic Planning

Performance Monitoring and Strategic Planning: Methodology, Data Needs, and Data Sources

Methodology	Data Needs	Data Sources
Assess the performance monitoring and planning systems used by the LEE. The key aspects to look into include: • Does the LEE have a business or strategic plan in place? If so, does it conduct operations and make investments in accordance with the plan? • Does the LEE have an ongoing performance monitoring system in place? • - If so, how were the goals established? How often do they evaluate performance against goals? How is the LEE doing overall in terms of meeting its goals/ targets? • - If they do not systematically evaluate performance, do they have an informal system for monitoring goals?	• Business Plan of LEE • Annual performance reports of LEE	• Interviews with LEE management and staff • Existing manuals, systems, and procedures • Existing internal and external reports

b. Human resource aspects

i. This component need to establish the following:

1. Does the LEE have adequate staff to effectively accomplish tasks?
2. Does staff at the LEE have the technical skills needed to do their jobs effectively?
3. Does the LEE have an effective human resources or training program for its staff?

ii. Assessment approach

1. Adequacy of Staff

Adequacy of Staff: Methodology, Data Needs, and Data Sources

Methodology	Data Needs	Data Sources
Assess the staffing levels and the ability to deal with human resources needs at the LEE. The key aspects to look into include: • Does the LEE have a human resources plan or manual? • Does the LEE have staff support to handle human resources development (hiring, firing, benefits, etc.)? • Are the staffing levels at the LEE perceived as adequate by staff and leadership? Can they accomplish day-to-day operations adequately? Can they respond in a timely manner to problems as they arise?	• Human resources plan or manual • Number of staff • Tasks required of staff	• Interviews with LEE management and staff • Existing manuals, systems, and procedures • Existing internal and external reports

2. Staff Competence

Staff Competence: Methodology, Data Needs, and Data Sources

Methodology	Data Needs	Data Sources
Assess the technical capacity or skills levels of the LEE. The key aspects to look into include: • Does the LEE have staff who are able to prepare annual and 5-year budgets? Do they do so? • Does the LEE have staff who are able to conduct projections of demand? Do they do so? • Does the LEE have staff who hold degrees or certifications relevant to the operations of the LEE?	• LEE annual reports • LEE budget proposals • Personnel files of LEE	• Interviews with LEE management and staff • Existing manuals, systems, and procedures • Existing internal and external reports

3. Human Resource Program

Human Resource Program: Methodology, Data Needs, and Data Sources

Methodology	Data Needs	Data Sources
Assess the LEE's human resources development or training programs. The key aspects to look into include: • Does the LEE conduct regular training of its employees? In what format (formal, classroom instruction, more informal and ongoing workshops, on- the-job training)? • Does the LEE require that its employees receive training on an ongoing basis? Does it provide incentives for staff who receive training? • Does the LEE require its staff to have degrees or certifications in relevant subject areas? If so, does it provide training or assistance in receiving these qualifications?	• Training plans and requirements • Records of actual trainings • Records of degrees and certifications	• Interviews with LEE management and staff • Existing manuals, systems, and procedures • Existing internal and external reports

4. Community aspects

   a. This component needs to establish the following:

      i. Are there any local cultural or social factors that inhibit demand for the LEE-provided good or service?

      ii. To what extent are LEE-provided good or service users aware of the need to make sufficient and timely payments to the LEE in order to keep receiving the good or service from the LEE?

   b. Assessment approach

      i. Demand Inhibitors

Demand Inhibitors: Methodology, Data Needs, and Data Sources

Methodology	Data Needs	Data Sources
Review secondary sources and consult local experts to ascertain the social and cultural factors that prevent the use of the LEE-provided good or service or inhibit demand for it. Determine any culturally mandated practices relating to use of the good or service. Break down the customer base or user population by segment or sub-group where appropriate. Also consider existing social and cultural factors that increase demand for services.	• Determinants of local demand for the LEE good or service	• Focus groups • Surveys • Interviews with community members, service provider staff, and local experts (e.g., CSO officers, academics) on social and cultural factors

ii. Payment compliance

Payment Compliance: Methodology, Data Needs, and Data Sources

Methodology	Data Needs	Data Sources
Review secondary sources and consult local experts to ascertain customer attitudes toward the service provider. The key aspects to look into include: • Do customers consider the LEE-provided good or service as adequate? • Do customers consider the price of the LEE-provided good or service fair? • Do customers think the price reflects the true cost of providing the good or service? • If the LEE is having difficulty covering the cost of the good or service it provides, do its customers know this, and are they sympathetic? Evaluate the extent to which attitudes are consistent across customer segments. • Are some customer segments less understanding than others?	• User payment compliance data	• Focus groups • Surveys • Interviews with community members, service provider staff, and local experts (e.g., NGO directors, academics) on social and cultural factors

APPENDIX F. CONDUCTING A FACILITY COST AUDIT FOR AN LEE

Purpose of Facility Cost Audit

The purpose of a facility cost audit for an LEE is not simply to collect cost data, but to provide LGU managers and officials with information they can use to make better management decisions in several areas:

- Analyzing the efficiency of service or good provision by the LEE;
- Making budget decisions affecting the LEE;
- Setting fees for goods and services provided by the LEE; and
- Choosing among alternative methods of providing the goods or services of the LEE, such as contracting.

The conduct of a facility cost audit entails four (4) basic steps. These are:

Step 1: Determine which LEE cost items are to be costed out

1. Ideally, all resources required to produce the LEE good or service must be included and fully costed.
2. To identify all resources used to provide a service, all areas of local government activity must be examined to determine which are used in some way to provide the LEE goods or services. These cost items may either be direct or indirect.

Examples of Direct Costs

Types of Costs	Category	Examples
Costs that can be readily and unequivocally attributed to a service or activity because they are incurred exclusively for that particular product/activity	Capital	Depreciation or lease costs of specific purpose buildings like hospitals; vehicles; computers; and other equipment used directly in delivering services
	Administrative	Transport; accommodation; and meal expenses for service delivery staff; service-related publications
	Materials & Supplies	Spare parts; inventory; fuel; office supplies used by service delivery department
	Labor	Salaries and wages of “works unit” employees; payments to contractors and service providers

Examples of Indirect Costs

Types of Costs	Category	Examples
Costs that are not directly attributable to an activity – often referred to as overheads	Capital	Depreciation or lease of main city hall building Depreciation and computer software license; maintenance fees of computers in the City Mayor's office
	Administrative	Cost of printing the State of the City Address
	Materials & Supplies	Supplies used by the City Mayor's Office
	Labor	Remuneration of the City Mayor and his staff

3. There is no single correct way to categorize a cost as direct or indirect. What is important is to:
    - Set reasonable guidelines to decide if a cost is direct or indirect.
    - Be consistent in categorizing costs as direct or indirect.
    - Count every cost, but only count it once.

Step 2: Get the cost audit organized

4. Organizing the cost audit

    4.1. Successful costing requires a team effort by department heads, employees, and LGU officials. Before any data is gathered, personnel involved in the study need to understand the purpose of the audit and their role in it.

    4.2. Audit guidelines shall be put in writing. These guidelines specify what information is to be collected, who is to collect it, sources of information to be used, and the assumptions underlying the study. Standard forms for collecting cost data also need to be prepared.

5. Time period to be covered by the cost audit

    5.1. If the goal of the audit is to determine the annual cost of providing a service, cost information will be needed for an entire fiscal year. However, the study need not be carried out over the whole year. Data from the most recent fiscal year can be collected and estimates made of subsequent changes in costs, or figures on current service levels and costs can be collected over a short time period and an estimate of yearly costs derived from them. For example, an LGU community wants to determine the full cost of operating its public market. Costs are found in the expenditure reports for the fiscal year just completed, and likely changes in current year costs are estimated.

    5.2. If the purpose of the study is to look at cost trends over a number of years – 3 to 5 years historical data. Past and current costs need to be collected, and estimates made of future costs.

6. Sources of cost figures for the cost audit

    6.1. The primary source of data is expenditure records in the audited financial books of accounts of the LGU.

6.2. Information is also contained in budgets and non-financial records such as equipment purchase and maintenance records, building records, mileage reports, and payroll and personnel records.

6.3. Costing requires that the expenses incurred to provide a good or service be calculated for the time period in which the good or service is provided, regardless of when the expenditures necessary to purchase these resources take place.

Step 3: Collect the cost information

7. After the cost audit has been defined and organized, the third step in the costing process is to collect the costs of the resources used to provide the service.

Step 4: Use the cost information

The purpose of the cost audit is not simply to collect cost information, but to use this information to make better management and policy decisions regarding an LEE.

8. Analyze the efficiency of good or service provision by the LEE.

   Efficiency means providing a good or service for the lowest possible cost. Cost information is used to answer a variety of points about good or service efficiency.

   a. <u>What makes the cost of providing the LEE good or service unusually high</u>? For example, the manager of an LEE sports center feels that the cost of materials used in recreation programs is high relative to other program costs. Costing helps to identify and explain these costs, so that the program manager can take corrective steps, if necessary.

   b. <u>Why have certain cost items changed?</u> For example, the utility cost of an LEE-operated sports center might have risen because of increases in power rates.

   c. <u>Have unit costs changed?</u> For example, the total operating costs of an LEE-operated sports center might have increased because of increased patronage, but in reality operating cost per user dropped.

   d. In analyzing service efficiency, it is important to <u>distinguish between the efficiency and effectiveness of services.</u> Efficiency means providing a service at the lowest possible cost, while effectiveness refers to the quality of the service and how well it is meeting its objectives. For example, the cost of municipal water service increases dramatically in one year, raising questions about its efficiency. However, further investigation reveals that a new purification system was installed during the year, which provides cleaner water. Thus, the water service is delivering a more expensive service, but one that better meets the need of citizens for pure water.

9. Make budget decisions

   In making budget decisions, LGU officials are interested in many of the issues of efficiency discussed above. In particular, year-to-year cost comparisons reveal changes in costs, while the breakdown between direct and indirect costs indicates which costs and departments relate directly to the provision of a good or service, and which are needed to support it indirectly. When changes in good or service provision levels are being considered, incremental and avoidable costs are important.

   - Officials may be asking a variety of costing questions when making budget decisions.
   - Why has the cost of the LEE-provided good or service changed from last year?
   - How can I justify to voters an increase in next year's budget for the provision a particular good or service?

- How much money can be saved if a particular service is reduced? How much will it cost to increase the provision of a good or service?

10. Set LEE pricing

    In order to determine the appropriate pricing for an LEE-provided good or service, LGU officials need to know the amount of good or service provided and the cost of one unit of the good or service. For example, the rental rates for public markets are based on average unit costs per sq. m. or the user fee for LGU swimming pools are based on average cost per user.

11. Choose among alternative methods of providing a good or service

    Avoidable and new costs are important factors in choosing among alternative methods of providing goods or services being provided by an LEE. For example, in considering privatization of the provision of an LEE-provided good or service, officials need to determine which costs the LGU or its private constituents will avoid and what new costs will be incurred if the contract is accepted. If avoidable costs are greater than new costs, then the contract offers financial savings to the town. If, on the other hand, avoidable costs are less than new costs, the change in service delivery does not offer financial savings.

APPENDIX G. FEASIBILITY STUDY OUTLINE

I. The Proponent

This section gives a description of the proponent local government unit.

A. The Local Government Unit (LGU)

1. Brief history
2. Brief socio-economic profile – population, economic base
3. Development trends and directions
4. Organizational chart of the LGU

B. Management and Organization

1. Organizational chart of the proposed LEE
2. Organizational linkages and arrangements if applicable

II. The LEE

This section provides a description of the LEE, its cost requirements, and source of financing.

A. Brief Description

1. Name of LEE
2. Purpose and justification of the need for such LEE
3. Economic contribution (relative to CDP economic goals and objectives)
4. Social relevance (relative to CDP social goals and objectives)

B. LEE Cost Estimates for First 10 Years of Operations

1. Capital expenditure requirements
2. Operating cost requirements

C. Proposed Method of Financing

1. Sources of financing
   a. Internal LGU sources (e.g., IRA, income from regular sources)
   b. External sources (e.g., national government grant, congressional grant, commercial bank financing)
2. In case of credit financing, identify collateral being offered (real property, chattel mortgage, project revenues, internal revenue allotment)

III. Technical Feasibility

This describes the technical aspects of the LEE.

A. LEE Site

1. Location of the LEE (approximate distance from Metro Manila or city center or other notable landmarks)
2. Land area
3. Building site
4. Vicinity map

B. Overall LEE Design

1. Conceptual design / artist's perspective / drawing
2. Facility design and layout
3. Production or service provision process and capacity

C. Input Requirements

Detailed cost of input requirements, e.g., raw material, labor, power and utilities

D. Project Timetable

Time frame/schedule of project implementation (date of start-up to start of operations) through a Gantt chart

E. Environmental Consideration

1. Measures/steps to be taken to minimize environmental damage
2. Sewage/waste disposal and management system
3. Approval by the Department of Environment and Natural Resources (DENR)

IV. Market Feasibility

This section shows an analysis of the market and marketing plan.

A. Market Analysis

1. Market trends
2. Historical and projected demand/consumption of the product or service
3. Projected demand/supply gap
4. Available complimentary/substitute product and services

B. Competition Analysis

1. Description of competitors
2. Advantages of proposed project over competitors

C. Marketing Plan

1. Target market
2. Market positioning
3. System of distribution

4. Promotions and publicity

D. Problems and Prospects of Proposed LEE

1. Favorable/unfavorable social, economic, and political development

2. Issues in LGU's locality which may affect the LEE

V. Financial Feasibility

This section provides information on the financial viability of the LEE.

A. Financial Assumptions

B. Projected Financial Statements (Income Statement, Balance Sheet, Cash Flow Statement)

C. Amortization Schedule in case of credit financing

D. Financial Viability Analysis

1. Discounted Cash Flow (DCF) Measures

a. Net present value (NPV)

b. Internal rate of return (IRR)

c. Benefit/Cost (B/C) ratio

2. Non-DCF Measures

a. Payback period

b. Accounting rate of return

APPENDIX H. FORMULA FOR COMPUTING THE FINANCIAL FEASIBILITY INDICATORS

1. Key Concepts

a. Discount Rate – interest rate that measures the "trade-off" between the present and the future – the so-called time preference rate.

b. Financial Discount Rate: financial rate of return foregone from the "best" alternative use of funds invested in the project. In practice this is measured by what is considered as the risk-free financial rate of return" measured by the Treasury Bill rate (usually) the 182-day rate + a margin to cover the costs of lending (usually 2.5 to 3%).

c. Time value of money is a critical consideration in financial and investment decisions. Money has a time value because of the opportunities for investing money at some interest rate.

i. Future value (FV)

A peso in hand today is worth more than a peso to be received tomorrow because of the interest it could earn from putting it in a savings account or placing it in an investment.

The FV of an investment (P) compounded annually at rate i for n years is:

$$\mathrm{FV} = \boldsymbol{P} \mathbf{\ x\ } \mathbf{(1 + \boldsymbol{r})^{\boldsymbol{n}}}$$

Example: PhP 1,000 placed in a deposit account earning 8% compounded annually will be 1,000(1+0.08) 4 = 1,000(1.3605) = PhP 1,360.50 at the end of 4 years.

ii. Present value (PV) – discounting

PV is the present worth of future sums of money

The process of calculating PVs or discounting is the opposite of finding the FV with the interest i called the discount rate.

$$\mathrm{PV} = \frac{FV}{(1 + i)^n}$$

Example: The PV of PhP 20,000 received 6 years from now at i = 10%

$$\mathrm{PV} = \frac{20{,}000}{(1 + 0.10)^6} = 20{,}000\ (0.5645) = \mathrm{PhP}\ 11{,}290$$

This means that receiving PhP 20,000 6 years from now is equivalent to receiving PhP 11,290 now at an annual discount rate of 10%.

2. Discounted cash flow (DCF) project financial feasibility indicators – considers the time value of money

a. Net Present Value (NPV)

$$\mathrm{NPV} = \sum_{t=0}^{N} \frac{B_t}{(1 + r)^t} - \frac{C_t}{(1 + r)^t}$$

b. Internal Rate of Return (IRR)

r at which NPV = 0

c. Benefit-Cost Ratio (BCR)

$$BCR = \frac{\sum_{t=0}^{N} \frac{B_t}{(1+r)^t}}{\sum_{t=0}^{N} \frac{C_t}{(1+r)^t}}$$

Where:

B_t and C_t are the annual cash inflows and outflows at market prices for the financial analysis and the annual economic benefit and cost streams for the economic analysis.

The discount rate r is the opportunity cost of the funds used in the project. For financial feasibility analyses of projects, the rate that is used is usually based on the "risk-free" 182-day Treasury Bill rate plus a 2.5 to 3% margin to cover the risk and costs of lending. As of end-December 2015, the 182-day Treasury Bill rate stood at 1.92%. Thus, the discount rate for LGU loans was set between 4.5 and 5.0% by banks lending to LGUs. The IRR is also referred to as the Financial Internal Rate of Return (FIRR) in financial analysis.

d. Decision Rule: Accept all projects meeting the following financial feasibility criteria.

i. NPV ≥ zero

ii. IRR ≥ r

iii. BCR ≥ 1

If a project–the benefits and costs of which are expressed in market prices–meets these feasibility criteria, then the project is said to be financially viable.

3. Non-DCF Project Financial Feasibility Indicators

a. Payback Period: length of time required to recover the amount of initial investment.

$$\text{Payback period} = \frac{\textit{Initial Investment}}{\textit{Increased Revenues}}$$

Example: Initial Investment = PhP 18,000 resulting in annual revenues of PhP 3,000.

Payback Period = **18,000/3,000** = 6 years

i. Decision Rule: Choose the project with the shorter payback period. The rationale is the shorter the payback period, the less risky the project, and the greater the liquidity.

ii. Advantages are: 1) it is simple to compute; and 2) handles investment risk effectively.

iii. Shortcomings are: 1) it does not consider the time value of money; and 2) it ignores cash flows after the payback period.

b. Accounting Rate of Return (ARR): measures profitability by relating the required investment to the future annual income.

Example: Initial investment is PhP 6,500, estimated life of 20 years, cash revenues per year of PhP 1,000, and annual depreciation of PhP 325.

$$ARR = \frac{1{,}000 - 325}{6{,}500}$$

i. Decision Rule: Choose the project with the higher rate of return.

ii. Advantages are: 1) it is easy to understand; and 2) recognizes the profitability factor.

iii. Shortcoming is that it fails to recognize the time value of money.

APPENDIX I. FREQUENTLY-ASKED QUESTIONS

1. ***Q: What local government unit (LGU) services qualify as local economic enterprises (LEEs)?***

   A: Section 17 of the Local Government Code (LGC) treats public utilities and economic enterprises separately. Economic enterprises are primarily concerned with public markets and slaughterhouses [See Section 17 (b)(2)(ix)]. The rest are treated as utilities and services. However, in the same Section, apart from markets and slaughterhouses, the phrase "and other enterprises" is added, which connotes that any other utilities or services can be considered as economic enterprise, provided they generate income or revenues. Given this legal ambiguity, any LGU service or utility may be considered as an LEE as long as they meet the qualification criteria in the case of proposed LEEs and comply with the legal provisions and other requirements governing LEEs.

2. ***Q: Are income-generating enterprises necessarily earning net income?***

   A: No. An enterprise may generate gross income, but the said income may not be sufficient for the enterprise to recover its costs and earn profit.

3. ***Q: What types of preparatory studies are needed for a proposed LEE?***

   A: A Feasibility Study (FS) and a 5-Year Business Plan (BP) are important to support a proposed LEE.

4. ***Q: What types of studies are needed for an existing LEE?***

   A: A 5-Year Business Plan will be prepared for each LEE. The BP will include a staffing plan and staff transition strategy such that, at the end of the 5th year, all personnel detailed or assigned to the LEE shall be reverted to their mother units and only full-time and contractual personnel hired to work on the LEE, chargeable against the LEE budget shall remain/shall be retained.

5. ***Q: Why is there a need for an FS before an LEE can be established?***

   A: The FS is needed in the establishment of an LEE to show proof of its economic/social viability in terms of demand and willingness and ability of the prospective users to pay for goods and services offered by the LEE. The FS also helps determine the LEE's potential for financial self sufficiency (100% cost recovery), and consequently, for its sustainability.

6. ***Q: Why is there a need to prepare a BP for an LEE?***

   A: The BP is a powerful management tool that details how the LEE is going to reach its objectives and where it plans to go. It covers all the relevant facets of LEE operations including management, staffing, marketing, and sales. As such, it serves as a guide to help the LEE attain financial self-sufficiency. For a proposed/new LEE, the BP will show how the LEE's potential for financial self-sufficiency can be realized.

7. ***Q: Who prepares the FS and corresponding BP for a proposed LEE and the BP for an existing LEE?***

   A: The LCE may assign or designate the appropriate personnel in the case of small-scale projects or hire an external consultant in the case of large-scale projects.

8. ***Q: What happens to the LCE-approved FS and BP?***

   A: For proposed LEE: Copies of the LCE-approved FS and BP shall be presented to the local sanggunian as bases for enacting the ordinance creating the LEE. The FS and BP shall also be appended to the budget proposal for the new LEE.

   For existing LEE: Copies of the approved BP of an existing LEE shall be appended to support the budget proposal for the continued operations of the LEE.

9. ***Q: What will serve as the legal basis for the creation of a new LEE?***

   A: A duly enacted ordinance creating the LEE based on the FS and BP approved by the LCE and presented to the local Sanggunian.

10. ***Q: Aside from the ordinance creating a new LEE, is a charter for the LEE needed?***

    A: There is no need for a separate charter. A duly enacted ordinance creating the LEE serves as the charter of the LEE.

11. ***Q: Can the ordinance creating a new LEE contain a provision specifying the term within which it should attain 100% financial self-sufficiency?***

    A: Yes, the ordinance can contain a provision which specifies a time period within which the LEE should achieve 100% financial self-sufficiency. Failure to achieve this within the specified time period will trigger proceedings implementing the exit strategies for the LEE, such as the enactment of an ordinance closing the LEE.

12. ***Q: Does an enterprise regarded by the LGU as an LEE need to be backed by an ordinance creating it as such?***

    A: Yes, the enterprise cannot be treated as an LEE unless legally created by an ordinance.

13. ***Q: What is the role of the local Sanggunian in the LEE start-up stage?***

    A: The Sanggunian enacts the ordinance creating the LEE. In the case of component LGUs, the ordinance will have to be reviewed by the appropriate provincial Sanggunian.

14. ***Q: What is a possible funding source for the preparation of the FS and BP?***

    A: The general fund budget.

15. ***Q: What reference materials are available to LGUs in the preparation of the FS and BP?***

    A: The Project Evaluation and Development (PED) Manual of the National Economic and Development Authority (NEDA) provides a good reference material.

16. Q: Who decides whether to engage in the direct provision of marketable goods/services, and how it can be set up to operate an effective LEE?

A: The LCE, based on the policy framework that will contribute to the quality service delivery goals of the LGU, may decide to set up, operate, and manage the LEE in accordance with a well-prepared FS and BP, with the authorization of the Sanggunian.

17. Q: What is the role of civil society in the LEE planning process?

A: Civil society forms a vital part of the Local Development Council which deliberates on the LDIP, which includes the LEE.

Financing the Proposed LEEs

18. Q: What reference material on financing sources are available to LGUs?

A: The Resource Mobilization Manual prepared by the Bureau of Local Government Finance is a useful guide for LGUs.

19. Q: What is the proper accounting treatment of the funds provided to the LEE for its operations?

A: Based on the Revised Chart of Accounts for LGUs prescribed under Commission on Audit Circular No. 2015-009 dated December 1, 2015, transfers to LEEs may be treated as advances or subsidies. The account due from LEEs is used to record the amount granted to LEEs maintained as special accounts in the general fund of the LGU, and is credited upon liquidation of the advance. The account subsidy to LEEs, on the other hand, is used to record fund transfers to economic enterprises from the general fund proper or other economic enterprises of the same LGU.

20. Q: Can an LEE avail of a loan directly from financial institutions?

A: An LEE cannot directly avail of a loan from financial institutions except when an LEE has a separate charter which allows it to directly borrow. In the absence of a charter, it is the LGU which avails of loans from financial institutions.

Costing Out and Pricing LEE Operations

21. Q: Does the local Sanggunian need to approve the prices of products and services of an LEE?

A: Yes. The prices of the LEE's product or services (or facility charges or users' fees) shall form part of the Ordinance creating the LEE.

22. Q: Are the LEE facility charges or users' fees part of the LGU's Local Revenue Code?

A: Yes. Under Section 5.3(j) of the LGC, LEE facility charges must be included in the LGU's Local Revenue Code as basis for collection. In case the LGU does not have a codified revenue code (legal document which comprehensively lists all LGU taxes, fees, and charges), an ordinance specifying the LEE fees and charges is sufficient.

23. Q: Who collects the users' fees and charges of LEEs — the local treasurer, or an LEE staff?

A: The local treasurer or his/her duly deputized and adequately bonded staff.

Pre-Budget Preparation

24. Q: Is it required that the LEE budget be linked with the LGU's Local Development Investment Program (LDIP) and Annual Investment Program (AIP)?

A: Yes. The setting up and operation of LEEs should be part of the LGU's development planning and investment programming. Thus, the LEE budget should be necessarily linked with the AIP and LDIP. Moreover, it should be noted that the LEEs are maintained as special accounts in the general fund. Thus, the LEE budgets are part of the general fund budget. As a matter of policy, the general fund budget should be based on the duly approved AIP.

Budget Preparation

25. Q: If the LGU has three (3) LEEs, how many budgets shall be prepared — only one for the LGU General Fund Budget including the three (3) LEEs, or a separate budget for the general fund and for each LEE?

A: LEEs are maintained as a special account in the general fund budget. Thus, while each LEE will have its own operating budget, the same forms part of the general fund budget which is authorized by one appropriation ordinance. In effect, regardless of the number of LEEs operated by the LGU, it will only prepare one general fund budget to be authorized under one appropriation ordinance.

26. Q: Is the LEE budget subject to the provision for Local Disaster Risk Reduction and Management Fund (LDRRMF)?

A: No. The budgetary requirement under Section 324(d) of the LGC, as amended by RA No. 10121 will not apply to the LEE budget because the LEE income is specific for LEE operations and not for regular LGU operations.

27. Q: Are budget calls for LEEs issued separately from the Budget Call for the General Fund Annual Budget?

A: No. The LCE may just issue one Budget Call to signal the preparation of the general fund annual budget and annual operating budget for each LEE, which forms part of the former.

Budget Authorization

28. Q: Is there a need to have a separate Appropriation Ordinance for LEEs?

A: No. The Annual Operating Budget of the LEE, which forms part of the general fund budget, shall be likewise authorized under the appropriation ordinance authorizing the general fund budget.

Budget Execution

29. Q: Who will maintain the Registries for each of the LEEs — the LGU accountant, or the budget officer, or an assigned staff of each LEE?

A: Since LEEs are maintained as special accounts in the General Fund, the Offices of the Local Budget Officer and Local Accountant shall be responsible for maintaining the books of accounts for the LEEs.

Budget Accountability

30. Q: Is the LGU required to prepare and submit separate Financial Reports for each LEE?

A: Yes, each LEE shall have its own Financial Reports separate and distinct from the general fund.

Performance Monitoring and Review

31. Q: What is the meaning of a financially self-sufficient LEE?

A: An LEE is considered financially self-sufficient if it generates revenues that entirely cover or exceed operating costs. Operating costs include personal services, maintenance and other operating expenses (MOOE) and financing charges. It should be noted that the corresponding capital outlay costs are also considered in determining operating costs because depreciation expenses are included as MOOE.

32. Q: What is the Semi-Annual Financial Self-Sufficiency Review (SAFSSR) and why should it be undertaken?

A: The SAFSSR is the semi-annual review and general examination of the costs incurred and the accomplishments attained vis-à-vis performance standards of an LEE.

It is undertaken to establish whether or not the LEE is proceeding towards financial self-sufficiency (or 100% cost recovery) and according to the Business Plan.

33. Q: When should the Semi-Annual Financial Self-Sufficiency Review (SAFSSR) be undertaken?

A: The SAFSSR will be undertaken six months after the start of operations for proposed/new LEEs. For existing LEEs, six months after the LEE has instituted necessary changes to comply with the legal requirements governing LEEs, as indicated under items 5.1.a to 5.1.i of this Manual.

34. Q: When does the LGU have to make a decision whether or not to continue LEE operations?

A: The LGU will decide whether or not to continue operating the LEE at the end of every 5-year period based on the Financial Self-Sufficiency Evaluation (FSSE) conducted at this time.

35. Q: What are the source documents for the FSSE?

A: The 10 SAFSSR reports corresponding to a 5-year period will serve as source documents for the FSSE. The SAFSSR reports, on the other hand, shall be based on the financial reports from the local accounting office.

36. Q: What will happen to LEEs which are able to attain 100% cost recovery or even net income?

A: If at the end of the 5-year period (covered by 10 SAFSSR reports) the LEE has attained 100% cost recovery or even net income, the LEE will be allowed to continue its operations.

37. Q: What will happen to LEEs which are not able to attain 100% cost recovery or have registered net loss?

A: If at the end of the 5-year period (covered by 10 SAFSSR reports) the LEE's cost recovery level is below 100%, a facility utilization audit and a facility cost audit shall be conducted by the designated LGU staff or consultant to see if the following three conditions for continued LEE operations are present: a) LEE services/products and facility patronage can be improved; b) facility users are willing and able to pay higher user fees that would cover the true cost of running the LEE; and c) increase in rates to recover the true cost of operating the LEE is socially and politically acceptable. As long as all of these conditions are met, the LEE shall be allowed to operate. A revised 5-Year business plan shall then be required to include measures to effect improved services/products and patronage and sustainability strategies. If not all of the three (3) conditions for continued LEE operations are present, the designated LGU staff or external consultant shall recommend an exit strategy for the LEE.

The LGU staff concerned may also recommend the suspension of operations for a specific period pending evaluation which exit strategy to undertake.

38. Q: What are the exit strategies which the LGU may consider?

A: Exit strategies include service shedding, closure, or divestment.

39. Q: What is service shedding?

A: Service shedding happens when the LGU stops the production/provision of selected LEE goods/services to concentrate on a few LEE goods/services.

40. Q: What is closure?

A: Closure is when the LGU shuts down LEE operations completely; however, provision of products/services may be continued through another mode other than LEE.

41. Q: What is divestment?

A: An LGU divests when it relinquishes either operational control or ownership to another entity, such as privatization. In relinquishing control, management can be bid-out to a private entity which is usually required to pay a minimum guaranteed annual or monthly payment. In relinquishing ownership, the LGU sells the LEE to another entity.

42. Q: What is the role of the Internal Audit Service/Unit (IAS/U) in LEEs?

A: The IAS/U may be tasked by the LCE to conduct a management audit of an LEE based on the SAFSSR findings of the LFC.

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