

Regulatory Reforms in the Water Supply Sector: An Inception Report

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BACKGROUND

Economic and resource regulation is a mandate of the National Water Resources Board (NWRB) as stated in the 1976 Water Code of the Philippines.¹

For resource regulation, NWRB has established a water permitting system that is implemented with the support of deputized agents. Other agencies such as the DENR-EMB and the LLDA also exercise resource regulatory functions particularly for water quality, allocation and user fees.

On the other hand, economic regulation has been a shared mandate with other institutions such as the LWUA, and other regulatory bodies created by contract (e.g. Subic Bay Water Regulatory Board, MWSS Regulatory Office and Other Economic Zones). In 2002, Executive Order 123 transferred the water tariff regulation function of the LWUA to the NWRB. However, full implementation has been impeded due to the current lack of technical and personnel capacity of NWRB.

Establishing an Independent Economic Regulatory Body for the Water Supply Sector

The need for an independent economic regulator for the sector has been acknowledged since the late 90's and yet, no unified, concerted effort to support the policy proposal has been mobilized. Renewed interest on this subject has come with the enactment of EO 279² calling for the establishment of an independent economic regulator for the water supply and sewerage sector.

¹ Presidential Decree No. 1067, A Decree Instituting A Water Code, Thereby Revising And Consolidating The Laws Governing The Ownership, Appropriation, Utilization, Exploitation, Development, Conservation And Protection Of Water Resources

² Executive Order 279, "Instituting Reforms in the Financing Policies for the Water Supply and Sewerage Sector and Water Service Providers and Providing for the Rationalization of LWUA's Organizational Structure and Operations in Support Thereof," February 2, 2004.

There have been several initiatives to push for the creation of new institutions to address the fragmentation and lack of coordination in the water sector. Two proposed legislations in particular have been filed before the 14th Congress (2007-2010), i.e., The Water Resources Management Act (WRMA) and the National Water Regulatory Commission (WRC). Both bills are still pending in Congress.

Current Regulatory Framework

The current regulatory framework in the Philippines is still in the process of developing as water services are provided under a number of different arrangements. Metro Manila's water supply is provided by the 2 concessionaires of MWSS as well as about 350 piped small scale water providers. Outside of Metro Manila, most water services are provided by 468 water districts (WDs) and 350 LGU run utilities. There are some privately run utilities including about 200 cooperatives, 150 RWSAs and 10³ private companies operating piped water systems in the provinces. Refer to **Figure 1** for the existing economic regulatory structures. The 3 primary economic regulatory agencies are the NWRB, LWUA⁴ and the LGUs. Overlaps in responsibilities are common.

NWRB. The private systems currently regulated by NWRB are systems operated by cooperatives, subdivision developers, homeowner associations, rural water associations, condominiums, private companies as well as non-piped water providers. EO 123 transferred the WD tariff approval authority to NWRB which to date still lacks the capacity and resources to exercise it.

LWUA. Although not established primarily as an economic regulator, LWUA had assumed a de-facto regulatory role given its functions and mandate expressly provided in PD 198 such as issuing standards for materials and operations, reviewing and approving water rates, and monitoring and evaluating performances of water districts. Even if EO 123 transferred the functions of tariff approval to NWRB, LWUA still provides some form of technical and institutional regulation. While EO 124 (1987) transferred the regulation of RWSAs to LWUA, the latter is not yet functioning as such. Consequently, most RWSAs are being regulated by NWRB.

LGUs. LGUs have the authority to regulate all forms of economic activities within their domain; hence their requirements for business permits, building design approval, health inspections, etc and legislative resolutions. Tariffs of LGU run systems are approved by the LGU's legislative bodies. However specifying levels of service and formulation of technical and operating standards are seldom, if ever, done by LGUs. Some LGUs have even submitted their tariff proposals to NWRB for approval.

Some industrial zones in the country, like the Subic Bay Metropolitan Authority (SBMA), have their own charters which gives them the authority to regulate economic

³ Balibago Water Company operates in 3 towns; 1 each in Bohol; Calapan,(Mindoro), General Trias, Cavite; 2 systems by Impart Engineering; Subic, Clark

⁴ Expressly provided in PD 198 is LWUAs authority to approve tariffs, set up and operating standards, and monitor conformance thereto.

activities within their jurisdiction. The SBMA established the Subic Bay Water Regulatory Board (SBWRB) while the Clark Development Corporation has an executive management committee.

Contract-Based Regulation

The MWSS tariffs are not subject to review by the NWRB.⁵ For this reason, when the MWSS operations were contracted out to 2 concessionaires, the concession contracts provided for the establishment of an MWSS Regulatory Office to regulate the 2 concessionaires.

Annex 1 shows the differing basis for tariff formulation by the different regulatory institutions. All these institutions are covered or formed by different laws or contracts, hence the differences. The current regulatory framework is as fragmented as can be gathered from Figure II.1 and Annex 1.

Existing Regulatory Instruments

The following is a list of laws and executive promulgations including their salient features which played a major impact on the roles of the 3 major government agencies with economic regulatory functions:

NWRB

Commonwealth Act No. 146 (1935): Also known as the Public Service Act, created the Public Service Commission to regulate private utilities and prescribed the Return on Asset methodology with 12% as the maximum return.

PD 1 (1971): Abolished the Public Service Commission and transferred its powers and functions to the Board of Power and Waterworks.

PD 424 (1974): Created the National Water Resources Council (NWRC), attached NWRC to the DPWH with the task of coordinating and integrating all activities related to water resource development and management.

PD 744 (1976) Directed the NWRC to eliminate all unnecessary regulatory measures and fees especially on privately owned and dug wells.

PD 1067 (1976): Promulgation of the “Water Code”. Updates and consolidates into one piece of legislation basic laws and administrative systems governing ownership, appropriation, utilization, exploitation, development, conservation and protection of the country’s water resources. The IRR of the Water Code was implemented in 1979.

⁵ Except when there is an appeal on tariff disputes.

PD 1206 (1977): Gave mandate for the regulation of private water supply systems from the defunct Board of Power and Waterworks of the Department of Energy to NWRC. Also made the NWRC an appeals body on tariff disputes arising between LWUA and the WDs.

EO 124-A (1987): Renamed the NWRC as the National Water Resources Board and reorganizes its Board to include heads of user agencies (MWSS, LWUA, NPC and NIA).

EO 123 (2002): Reorganized the Board membership; attached NWRB to the DENR and transferred the review and approval of WD tariffs to NWRB from LWUA.

The Board and the NWRB Secretariat have been provided with a clear mandate for resource management. It has the power to issue water permits for water abstraction outside of domestic use, impose fees thereof, and penalties for violation. While the GOP has enunciated formal and comprehensive policies for the comprehensive development, utilization, conservation and protection of water resources, the NWRB is however unable to exercise fully its coordination and review function. No review other agency's plans was done; neither did NWRB have the authority to influence compliance from the line agencies.

There is still a lack of adequate or unifying legal provisions for economic regulation. The basis of tariff approval by the NWRB is still the Public Service Act of 1935 and is applied only to private utilities.

To address this problem, the NWRB did something on its own to beef up its capacity for both resource and economic regulation. It enlisted the support of donor agencies for a series of studies in this direction, starting in 1995. A partial list includes: **i)** UNESCAP advisory service in the preparation of a Manual on Guidelines and Procedures in Water Resources Management in the Philippines; **ii)** Technical Assistance Study on the Strengthening of NWRB is completed in response to the recommended reforms stated in the NEDA Board Resolution No. 4 (1995); **iii)** Water Resource Management Study for Angat Reservoir; National Water Data Collection Networks (NWDCN) for streamflow, groundwater and water quality; design and establishment of a National Water Information Network (NWIN) as a computer-based system to link the database of collection agencies (1997); **iv)** workshop on Institutional Strengthening of NWRB (2000); **v)** Formulation of revised organizational Structure (2003) ; **vi)** ADB Study on Tariff Methodology for Private Utilities under NWRB (2004); **vii)** PAHRDF's Integrated Quality Management Program; and **viii)** "Towards an Integrated Water Resource Management" TA from GTZ (2007).

As a result of the promulgation of the Water Code, NWRC manpower was increased from 45 in 1974 to 167 in 1983. After transferring the additional function of WD tariff review to NWRB, the current staff complement is 100 with limited financial resources.

LWUA

PD198 (1973): This law authorized the formation of Water districts in the provinces on a local option basis and created the LWUA as a specialized lending institution with authority to review WD tariffs. Rates must be adequate to provide for the following: i) cost of services and meters; ii) annual operating expenses; iii) maintenance and repair of waterworks; iv) a reasonable surplus; v) debt service; and vi) sinking fund.

LOI 700 (1978): Directed LWUA to approve warranted tariff increases up to a maximum of 60% of existing tariffs. Directed the WDs to conduct public hearings prior to any tariff adjustment.

LOI 744 (1978): Directed LWUA to adopt ways and means to reduce WD tariffs.

EO 124 (1987): Abolished the RWDC and transferred to LWUA the supervision and development of the RWSAs.

EO 123 (2002): Transferred LWUA's authority to review WD tariffs to the NWRB.

EO 279 (2004): Rationalized LWUA's organizational structure in support of new sector financing policies. LWUA to finance only WDs below creditworthy status.

While the guidelines for WD tariff review may have been sufficient, there is a lack of emphasis on setting coverage levels. LWUA does not set or enforce WD coverage levels. While the law mandates LWUA to set and enforce operating standards, LWUA has set up only 3 operating standards⁶. This may be partly due to LWUA's conflicting roles of a regulator, technical advisor and a financing institution.

Local Government Units/DILG

RA 7160 of the Local Government Code of 1991 gave more autonomy, powers, resources and responsibilities to the LGUs as the national governments partner in attaining national goals. This Act promoted greater autonomy and self-reliance to LGUs for the provision of basic services to its constituents.

To make LGUs responsive to their new mandate, DILG together with the MDFO set up many capacity building programs for LGUs. While some gains have been made in some LGUs, most LGUs either do not have the capacity or are constrained by their political environment to perform economic regulation functions.

The mandate to regulate tariffs charged by LGU units is provided for by the powers given to LGU by the RA 7160 and the mandate of NWRB. Under the Public Service Act of 1935, government utilities were not required to secure CPCs from the Public Service Commission, but may be regulated with respect to tariffs like private

⁶ NRW, staff to connection ratio and collection efficiency.

utilities. It is not clear if that provision was repealed or amended by RA 7160. Presently NWRB regulates LGU run utilities on a voluntary basis only.⁷

THE CHALLENGE OF REFORMS

Review of Proposed Legislations

Two pieces of legislation have been proposed for a single economic regulatory body for the water sector. They are:

1. Water Resources Authority of the Philippines (WRAP)

In August 1997, the Presidential Task Force on Water Resources Management and Development (PTFWRDM) drew up a legislative proposal to create a new apex body to take charge of water resources management and economic regulation of all utilities within the country. The proposal seeks to create the WRAP as a new entity to take over the functions, powers and responsibilities of the NWRB, in addition to new and broad powers and functions expressly granted to it under the measure.

This proposed legislation was drafted in 1997⁸ and spearheaded by the PTFWRDM⁹ under the DENR. Certified as a priority measure by President Ramos in 1997, and sponsored by Sen. Flavio and Rep. Acosta, the bill was left pending at the committee level by the time 10th Congress (1995 – 1998) adjourned. It was re-filed during the 12th Congress (2001 – 2004) and 13th Congress (2004-2007) but it never got to the committee hearing stage. The task force was disbanded in 2002.

A new WRAP bill is now in the legislative mill of the 14th Congress (2007-2010). Sponsored by Senator Revilla Jr as SBN 799, the bill is with the Public Service Committee of the Senate. **Annex 2** shows some salient provisions of SBN 799.

2. Water Regulatory Commission (WRC)

The WRC proposal was initiated in 1996 by DPWH¹⁰ to develop an independent economic regulatory body distinct from water resource regulation which would remain with the NWRB.

This WRC proposal was not filed during the 10th and 11th Congress. During the 12th Congress (2001-2004), the measure was filed in the lower house but never reached the Committee hearing stage. No attempt was recorded during the 13th Congress.

⁷ As of end 2007, 6 LGUs have submitted tariffs to NWRB for approval.

⁸ With funding from UNDP

⁹ Presidential Task Force on Water Resources Development and Management

¹⁰ With funding from IBRD

During the 14th Congress (2007-2010), Sen. Estrada filed SBN 518 which proposed to create the WRC. SBN 518 has been referred to 2 Senate committees where it remains pending. **Annex 3** shows some provisions of SBN 518.

Both the WRAP and WRC bills intend to strengthen the country's economic regulatory framework but the underlying principles are divergent. While the WRC separates the resource regulatory function from economic regulation, the WRAP proposes to create an apex body incorporating both functions. Both bills were drafted at almost the same period, but were championed by 2 different executive departments and funded by 2 different donor agencies.

Sadly, during the 14th Congress, these 2 conflicting bills (WRAP and WRC) have been re-filed at the same time, reinforcing non-agreement among the water stakeholders.

To be able to move forward, the major stakeholders in the sector must agree on the end result. The existing fragmented regulatory framework in the country needs a unifying law which will spell out the principles, rules and instruments for economic regulation for all utilities in the country. Whether to combine it with water resource management or not is another issue that must be resolved.

Lessons from the Energy Sector

RA 9136, otherwise known as the Electric Power Industry Reform Act (EPIRA) was enacted by Congress in 2001 in response to a power crisis at that time. The EPIRA law is an omnibus bill which consolidated House Bill 8457 and 4 Senate bills and contains the following key provisions: i) privatization of NPC; ii) creation of TRANSCO; iii) creation of the Energy Regulatory Commission (ERC); iv) creation of PSALM; v) strengthening of the NEA; vi) strengthening of electric cooperatives; and vii) creation of the Congressional Power Commission.

The EPIRA law was a response to an energy crisis which reached its peak during the late 90s. The draft bill was submitted to Congress by President Ramos, went thru President Estrada's administration and was finally signed by President Macapagal-Arroyo on 8 June 2001, 4 days after Congressional approval.

An analysis of the EPIRA law and its process reveals that all institutions in the energy sector have been strengthened. The law consolidated 5 complementary energy bills pending in Congress at that time.

To be successful in this endeavor, the water stakeholders must not push for conflicting concepts in the regulatory framework.

GOING FORWARD

To achieve the objectives of having an appropriate regulatory framework for water supply and sanitation (WSS), the following steps are recommended:

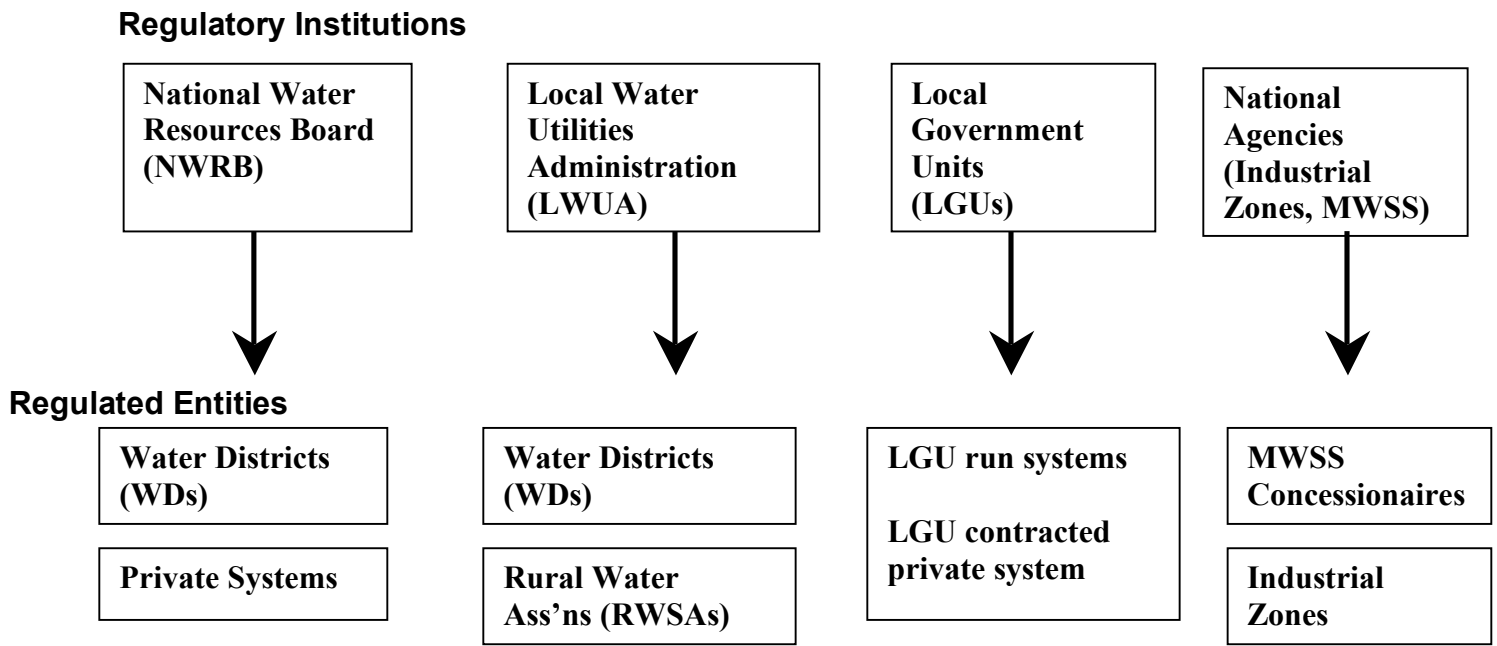
1. The major stakeholders must agree or determine the appropriate institutional set-up —separate economic and water resource regulatory bodies or a combined institution.
2. In connection with (1) above, consultations with the different stakeholders for information dissemination and consensus building activities should be undertaken. The major stakeholders to be consulted are the DILG and the LGUs, the LWUA and its WDs, and the NWRB with its private water providers. The different donor agencies can then be approached to help in the conduct of the different consultation workshops in order to make it a really unified undertaking of the sector.
3. A draft bill can then be drawn up which can then be presented to multi stakeholder conferences for further discussion, obtain concurrences or consensus and minimize possible objections. Water champions both in the executive and legislative branches can then be selected to coordinate efforts.
4. The proposed measure can then be presented to the NEDA Board for approval and endorsement to the President for priority certification to Congress.
5. Information dissemination workshops for Congress sponsors should be done to apprise them of the current situation and the bill's urgency. If necessary, a withdrawal of one of the current bills filed should be done.
6. Gathering of mass support or bill endorsements to Congress.

Items 1-3 can be done up to the month of August 2008. Simultaneous with steps 2–6, a study of necessary executive issuances for strengthening economic regulations can be pursued.

There are a number of institutions with regulatory responsibilities including NWRB, LWUA and the LGUs. The Subic Bay Water Regulatory Board is a special regulatory

unit created by the SBMA which can be considered either as an LGU unit or a national agency. Specialized regulators such as the MWSS-RO are either authorized by charters of the different agencies or created by contracts. Within the existing structure, there are differences in regulatory practices, processes and fees and cases of overlapping functions or jurisdictions.

Figure II.1 Water Economic Regulatory Institutions



NWRB

While EO 123 gave tariff approval of WDs to NWRB, the same has not been effected due to lack of capability and resources within NWRB. The private systems currently regulated by NWRB are systems operated by cooperatives;, subdivision developers, homeowner associations, rural water associations, condominiums, private companies as well as non-piped water providers.

LWUA

EO 123 transferred only the function of tariff approval to NWRB. LWUA still provides some form of technical and institutional regulation. While EO 124 (1987) transferred the regulation of RWSAs to LWUA, most RWSAs are also being regulated by NWRB, as LWUA has not focused on this role.

References

Action Plan for Reforms Relating to the NWRB; Final Report by the NWRB Team, IBRD; Dec 1995

Amended PD 198 and Other Related Issuances, by the LWUA

Provincial Towns Water Supply and Sanitation Program (PTWSSP) Main Report, by KFW; 2004

Rationalizing Tariffs under NWRB, Final Report by IDP Consult, ADB PDA; Feb 2005

Senate Bills 799 and 518

RA 9136, Energy and Power Industry Reform Act, 2001

Introduction to Economic Regulation of Water Supply and Wastewater Utilities; by Stone and Webster Consultants, ADB, 2004

Sustainability of Community-Based Rural Water Supply Organizations; by A. de Vera, WSP-IBRD, 2000

Annex III.1 Regulatory Agencies & Tariff Methodologies

Government Agencies

NWRB – Return on Assets

LWUA – Cash Flow

Contract Based Regulators

MWSS-RO – Return on Investments with Appropriate Discount Rate (ADR)

SBWRB - Return on Equity

CDC - Internal Rate of Return

LGUs – Cash Flow and Political Considerations

Annex III. 2 Major Provisions of SBN 799 (WRAP Bill)

1. Creation of the **Water Resources Authority of the Philippines (WRAP)** with the following functions:

- a) Formulation of a national framework for integrated and sustainable water resource development;
 - b) Formulation of water data and information system and rationalization of the data collection activities of all agencies in the sector;
 - c) Issuance of water permits for all inland water and the imposition of raw water fees.
 - d) Issue operating licenses to monopoly suppliers of water/sewerage and irrigation services; only registration requirements for all non-monopoly service providers.
 - e) Licensing of well drillers;
 - f) Exercise all powers given to NWRB; and,
 - g) To regulate all LWUA approved WD tariffs.
2. **Organization.** The new office shall be attached to the Office of the President and headed by a Director-General (DG). A 3-man **Water Resources Adjudication Board** shall be created under the DG office to exercise appellate jurisdiction adjudicate over decisions of the Authority's adjudication officers. A **Water Resources Consultative Council** shall be established in every regional or basin field office to act as an advisory council.
 3. Provision of fines and imprisonment penalties for violators of the Act. The WRAP can suspend or revoke operating licenses, issue cease and desist orders, and can order compensation for damage to water sources.
 4. Funds collected from fees, fines and others shall be retained by the Authority.

Annex III.3 Salient Provisions of SBN 518 (WRC Bill)

1. Creation of the **Water Regulatory Commission (WRC)** which shall be attached to the office of the President and headed by a 3-man collegial body headed by the Chairman (Secretary rank) and 2 Associate Commissioners (Usec rank). The Commission shall appoint a Executive Director who shall be the Chief Operations Officer of the agency.
2. Powers and Functions of the Commission
 - a) Formulation of Rules to facilitate and rationalize the efficient provision of piped water and sewerage services;
 - b) To formulate a tariff methodology. Approve and regulate tariffs of all licensees for piped water /sewerage services;
 - c) To issue, suspend or revoke licenses for piped water/sewerage providers. The utilities covered are all piped public and private systems to include LGUs and WDs.
 - d) To provide a system for complaints and appeals related to the tariffs and services provided by licensees;

- e) To charge an annual levy and reasonable fees, fines & surcharges to all licensees;
 - f) To provide a system for dispute settlement among its licensees;
 - g) Provide service efficiency standards and monitor annual performance of licensees.
3. All orders, rules or decisions made by the Commission are appealable only to the Court of Appeals.
 4. The bill proposes fines and/or imprisonment for violations.