Report Number: ICRR0022564

## 1. Operation Information

| Operation ID | Operation Name |
|---|---|
| P167651 | Improving Fiscal Management |
| **Country** | **Practice Area (Lead)** |
| Philippines | Macroeconomics, Trade and Investment |

**Non-Programmatic DPF**

| L/C/TF Number(s) | Closing Date (Original) | Total Financing (USD) |
|---|---|---|
| IBRD-89320 | 31-Mar-2020 | 450,000,000.00 |
| **Bank Approval Date** | **Closing Date (Actual)** | |
| 15-Mar-2019 | 31-Mar-2020 | |

| | IBRD/IDA (USD) | Co-financing (USD) |
|---|---|---|
| Original Commitment | 450,000,000.00 | 0.00 |
| Revised Commitment | 450,000,000.00 | 0.00 |
| Actual | 450,000,000.00 | 0.00 |

| Prepared by | Reviewed by | ICR Review Coordinator | Group |
|---|---|---|---|
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## 2. Program Objectives and Pillars/Policy Areas

### a. Objectives

The program development objective of the Philippines Improving Fiscal Management Development Policy Loan was "to improve fiscal management with three development objectives: (a) strengthening tax policy; (b) enhancing public finance management and budget planning; and (c) strengthening fiscal risk management of public assets."

### b. Pillars/Policy Areas

The program supported three policy areas and five prior actions (Loan Agreement, page 5).

**Pillar 1 - Strengthening Tax Policy** aimed to increase the revenue potential of the economy and the economic efficiency of tax policy by taking regulatory measures against tax base erosion.

- **PA1.** The Government has increased the excise tax on petroleum products.
- **PA2.** The Government has expanded the value-added tax (VAT) tax base by repealing special laws with non-essential VAT exemptions.

**Pillar 2 - Enhancing Public Financial Management and Budget Planning** aimed to strengthen budget planning and budget execution by improving the central government budget management system and improving the predictability of the budget.

- **PA3.** The Government implements a centralized budget management system as part of its adopted budget reform agenda.
- **PA4.** The Government has shifted from obligation-based budget planning and execution to a one-year cash appropriation for the national budget.

**Pillar 3 - Strengthening Fiscal Risk Management of Public Assets** aimed to strengthen the resilience of fiscal operations to climate and disaster risks by formulating and implementing a policy for the financial risk management of public assets, establishing an institutional framework for the financial risk management of public assets, and structuring financial instruments that insure against the financial risks to public assets.

- **PA5.** The Government is implementing a policy for comprehensive financial risk management of public assets against disasters, by setting up the required institutional infrastructure and putting in place financial instruments that insure key assets.

### c. Comments on Program Cost, Financing and Dates

Program Cost. The program was estimated to cost US$450 million at appraisal.

Financing. The program was financed by a loan of US$450 million from the IBRD.

Dates. The program was approved on March 15, 2019, became effective on May 24, 2019 and closed as scheduled on March 31, 2020.

## 3. Relevance of Design

### a. Relevance of Objectives

**Relevance to Government Priorities.** The program objectives were relevant to the development priorities advanced by the Philippines in response to these challenges.

- The government launched the Comprehensive Tax Reform Program (CTRP) in 2016 to: (a) make the country's tax system more equitable, efficient, and competitive, and (b) generate sufficient revenue to finance the country's socioeconomic development agenda. The CTRP consisted of six tax reform packages in support of the country's inclusive growth strategy, each of which focused on a different area of tax policy and aimed to achieve targets related to revenue generation, economic efficiency, and fiscal equity.
- The first of six tax reform packages under the CTRP, the Tax Reform for Acceleration and Inclusion (TRAIN), was passed by Congress and signed into law (Republic Act 10963) in 2017 and became effective in 2018. TRAIN reduced personal income tax rates; adjusted the estate and donor's tax; broadened the VAT base by limiting exemptions; adjusted excise taxes on tobacco, automobiles, oil, and mineral products; and introduced an excise tax on sugar-sweetened beverages and cosmetic procedures. The first policy area under this development policy operation (strengthening tax policy) and the two prior actions under this pillar (increase the excise tax on petroleum products and expand the VAT tax base by repealing special laws with non-essential VAT exemptions) supported two priorities under TRAIN – adjust excise taxes on tobacco, automobiles, oil, and mineral products, and broaden the VAT tax base by limiting exemptions.
- To complement reforms in fiscal revenues, the government prepared separate draft legislation in 2017 to advance reforms in fiscal expenditures. The proposed Budget Modernization Act aimed to: (a) modernize the public budgeting system; (b) accelerate program delivery; and (c) strengthen accountability. The law would establish an annual appropriations system on a cash basis (instead of expenditure obligations); strengthen cash flow management by implementing the Treasury Single Account (TSA); and establish the Office of the Comptroller General. A tool for government cash management, the TSA is a unified structure of government bank accounts that enable the consolidation and optimum utilization of government cash resources. The second policy area under this development policy operation (enhancing public financial management and budget planning) and the two prior actions under this pillar (implements a centralized budget management system, and shifts from obligation-based budget planning and execution to a one-year cash appropriation) supported two priorities under the proposed Budget Modernization Act – adjust excise taxes on tobacco, automobiles, oil, and mineral products, and strengthen cash flow management by implementing the TSA and establishing an annual appropriations system on a cash basis.
- The government also pursued a comprehensive approach to mitigating fiscal risks, by better managing the costs of frequent and large climate shocks and natural disasters that were often borne by the national government budget (for the reconstruction of destroyed core assets, which often did not have or had inadequate insurance coverage). With support from development partners, the government developed the Disaster Risk Financing and Insurance Strategy in 2015, which aimed to sustain economic growth by protecting public finances against the economic damage and fiscal costs of natural disasters. The third policy area under this development policy operation (strengthening fiscal risk management of public assets) and the prior action under this pillar (implement a policy for comprehensive financial risk management of public assets against disasters, by setting up the required institutional infrastructure and putting in place financial instruments that insure key assets) supported two priorities under the Disaster Risk Financing and Insurance Strategy – protect against the economic damage and fiscal costs of natural disasters..

**Relevance of Bank Group Strategy.** The program objectives were consistent with the Bank Group's strategy in the Philippines.

- At program appraisal, the program objectives were aligned with the "engagement areas" of the *Country Partnership Strategy for the Republic of the Philippines for the Period FY2015-2018* (CPS). The first and second program objectives were aligned with the first outcome, "strengthened public finances, fiscal transparency and financial accountability," under the first engagement area, "Transparent and Accountable Government," of the CPS. The third program objective was aligned with the first outcome, "increased physical and financial resilience to natural disaster and climate change impacts," under the fourth engagement area, "Climate Change, Environment, Disaster Risk Management" of the CPS.
- At program closing, the program objectives were aligned with the "focus areas" of the *Country Partnership Framework for the Republic of the Philippines for the Period July 2019-December 2023* (CPF). The first and second programs objectives were aligned with the fourth objective, "improved budget execution and revenue management," under the second focus area, "Competitiveness and Economic Opportunity for Job Creation," of the CPF. The third program objective was aligned with the tenth objective, "increased resilience to natural disasters and climate change," under the third focus area, "Addressing Core Vulnerabilities by Building Peace and Resilience," of the CPF.

## b. Relevance of Prior Actions

### Rationale

The program defined five prior actions to achieve the program objectives.

**Relevance of Prior Actions for Pillar 1 - Strengthening Tax Policy**

- <u>Causal Chain</u>. Part of the first of the CTRP, the adjustment of excise taxes on petroleum products and the elimination of non-essential exemptions to the VAT would address tax policy problems associated with the decline in the real value of excise taxes (.
- **PA1** (increase the excise tax on petroleum products) was informed by *Tax Policy Notes for More Inclusive Growth: Inputs to the New Administration (2016)* and analytic and advisory services delivered under the Game Changers for Inclusive Growth Program (2016-2020). The results chain was convincing. Increasing the excise tax on petroleum products would help boost tax revenues. Excise taxes had been fixed in nominal terms in the Philippines since 1997. Consequently, the real value of excise taxes had been greatly reduced with inflation. In the case of the excise tax on petroleum products, the substantial increase in gasoline and diesel prices since 1997 had greatly reduced the real value of the excise tax; the tax burden on the excise tax for gasoline fell from 46 percent in 1997 to 9 percent in 2013 (the decline was even more pronounced for diesel). The prior action would make a major contribution to the achievement of the objective to strengthen tax policy. The increase in the excise tax would not only help boost tax revenues. With almost 60 percent of fuel and lubricants consumed by the top income decile, the decrease in the burden of fuel taxes had had a regressive redistributive incidence. Under this tax reform plan, part of the additional tax revenues from the tax increase would be earmarked for human capital and social investment, including for the Unconditional Cash Transfer program. The relevance of this prior action is rated satisfactory.

- **PA2** (expand the VAT tax base) was informed by *Tax Policy Notes for More Inclusive Growth: Inputs to the New Administration (2016)* and analytic and advisory services delivered under the Game Changers for Inclusive Growth Program (2016-2020). The results chain was convincing. The efficiency of the VAT in the Philippines was low, partly reflecting the large number of exemptions. VAT efficiency was 35 percent, compared to the average of 40 percent in the ASEAN and 63 percent in the East Asia and Pacific region. The prior action would make a major contribution to the achievement of the objective to strengthen tax policy. The reform would repeal 54 of 61 special laws that had granted non-essential VAT exemptions. At the same time, VAT exemptions that protected the poor and vulnerable would be preserved. The relevance of this prior action is rated satisfactory.

**Relevance of Prior Actions for Pillar 2 - Enhancing Public Financial Management and Budget Planning**

- <u>Causal Chain</u>. The shift from an obligation-based to a one-year cash-appropriation-based national budget and the deployment of a new budget and treasury management system would address public financial management problems associated with the intermingling of continuing-year and current-year appropriations and the lack of an integrated accounting and monitoring system. The cash-appropriation-based national budgeting system would impose internal discipline in the execution of expenditures, while the new budget and treasury management system would strengthen the internal control of payments and facilitate better monitoring of budgets.
- **PA3** (implement a centralized budget management system) was informed by: the *Public Expenditure and Financial Accountability Assessment (2016); Support to Identify and Develop Strategies to Scale up Budget Execution and Provide Front-Line Service Delivery* (2017); *Reimbursable Advisory Services Supporting Public Financial Management in the Philippines, 2018-2019*; and the *Public Investment Management Assessment* (IMF and World Bank, 2018). The results chain was convincing. A centralized budget management system – the Budget and Treasury Management System (BTMS) – would help address weaknesses in public financial management. According to the *Public Expenditure and Financial Accountability Assessment* (2016), weaknesses in public financial management were affecting budget transparency and reliability. The assessment found that "the lack of an integrated computerized system contributes to the difficulty in consolidating and reporting information in a timely manner. Reconciliations between the records of the recipient unit and the downloading entity are often delayed. These deficiencies constitute a major continuing public financial management impediment and can only be addressed through developing a comprehensive, distributed, integrated accounting and performance information system. Such an investment would provide substantial returns in improvements in fiscal discipline and efficient service delivery against government intentions for its programs." The relevance of this prior action is rated satisfactory.
- **PA4** (shift from obligation-based to a one-year cash appropriation-based national budget) was informed by: the *Public Expenditure and Financial Accountability Assessment (2016); Support to Identify and Develop Strategies to Scale up Budget Execution and Provide Front-Line Service Delivery* (2017); *Reimbursable Advisory Services Supporting Public Financial Management in the Philippines, 2018-2019*; and the *Public Investment Management Assessment* (IMF and World Bank, 2018). The results chains were convincing. The *PEFA Assessment (2016)* found that "using continuing appropriations that are difficult to identify separately in the accounting system reduces the clarity of the budget because the expenditures remaining are not disaggregated between those covered by the current year appropriations and those incurred against continuing appropriations from previous years. The present degree of budget reliability does not provide the Government with a budget that is reliable enough to provide fiscal discipline and for agencies to plan the effective provision of services." The annual appropriation system provided authority to incur obligations during the year, as a firm commitment of funds for the procurement of specific goods or services, with the actual contract

completion taking many months after obligation. The prior action would make a major contribution to the achievement of the objective to enhance public financial management and budget planning. The obligation-based appropriation therefore provided limited discipline in execution of expenditure within the budget year and introduced unpredictability in cash management. The relevance of this prior action is rated satisfactory.

**Relevance of Prior Actions for Pillar 3 - Strengthening Fiscal Risk Management of Public Assets**

- Causal Chain. Creating a registry of public assets managed by a new Office of Public Asset Registry and testing an indemnity-based insurance program for high-risk government assets would begin to lay the foundations for the management of fiscal risks related to the destruction of, and damage to, public assets due to natural and climate disasters Better fiscal risk management, in addition to improved public budget management and stronger tax revenue mobilization, would enable the government to better deliver on the nation's public investment program.
- **PA5** was informed by: *Financial Protection Against Natural Disasters: An Operational Framework for Disaster Risk Financing and Insurance* (2014); *Improving Public Assets and Insurance Data for Disaster Risk Financing and Insurance Solutions - Technical Contribution to the Asia Pacific Economic Cooperation Finance Ministers' Process* (2017); *Developing a Public Asset Registry for the Philippines - Inventory and Conceptual Design* (2018); *Managing Disaster-Related Contingent Liabilities in Public Finance Frameworks - Technical Contribution to the APEC Finance Ministers' Process* (World Bank and OECD, 2018); and *Supporting the Implementation of the Disaster Risk Financing Strategy of the Government of the Philippines, 2014-2018* (2018). The results chain was convincing. The Philippines incurred regular and significant losses to public and private assets as the result of frequent typhoons and earthquakes. At the same time, public assets were either uninsured or under-insured. The *PEFA Assessment (2016)* cited weaknesses in public asset management and reporting, noting that each agency managed its own non-financial assets. The Commission on Audit consolidated the available information in its Annual Financial Report showing the balances on different non-financial assets, but the accuracy of the data was doubtful. The establishment of a comprehensive public asset registry would be key first step toward improving public asset management and insurance against natural disasters and climate risks. The reform included the creation of a new office of Public Asset Registry at the Bureau of the Treasury, a vital institutional measure for better asset management. The institutional reforms would be complemented by a pilot indemnity-based insurance program (an insurance policy that compensates an insured party for certain unexpected damages or losses up to a certain limit – usually the amount of the loss itself), under the oversight of the Bureau of the Treasury, for strategic high-risk national government assets. The relevance of this prior action is rated satisfactory.

### Rating

Satisfactory

## 4. Relevance of Results Indicators

### Rationale

The operation defined five results indicators.

| RI (number and description) | Associated Prior Actions | Baseline / Target | Status |
|---|---|---|---|
| **Pillar 1: Strengthening Tax Policy** | | | |
| **RI1**: Revenue from the petroleum excise tax | PA1 | Baseline: 0.2 percent of GDP (2017) Target: At least 0.5 percent of GDP (2019) | Actual: 0.7 percent of GDP (2019) |
| **RI2**: Revenue from the VAT | PA2 | Baseline: 4.3 percent of GDP (2017) Target: At least 4.6 percent of GDP (2019) | Actual: 4.5 percent of GDP (2019) |
| **Pillar 2: Enhancing Public Financial Management and Budget Planning** | | | |
| **RI3**: Share of payments processed through the BTMS | PA3 | Baseline: 0 percent of payments (by value) are processed through BTMS (2017). Target: At least 10 percent of payments (by value) are processed through BTMS | Actual: 30 percent (2019) |
| **RI4**: Deviation between the annual budgets approved by Congress and executed yearly budget | PA4 | Baseline: Disbursements were 68.5 percent of total funds approved by Congress for the most recent completed budget year 2017 Target: Disbursements are more than 80 percent of funds approved by Congress for budget year 2019 | Actual: 84 percent (2019) |
| **Pillar 3: Enhancing Fiscal Risk Management of Public Assets** | | | |
| **RI5**: Number of departments / national government agencies, with data captured in the National Asset Registry | PA5 | Baseline: Zero departments / agencies have data captured in a National Asset Registry (2017). Target: At least 5 departments / agencies (Department of Education ; Department of Health; Department of Public Works and Highways ; National Irrigation Administration ; and Department of Social Welfare and Development) will have data captured in the National Asset Registry by end-2019 | Actual: Five government agencies (DOE, DOH, DPWH, NIA, and DSWD) had their assets listed in the National Asset Registry (2019) |

**Relevance of Results Indicators for Pillar 1 - Strengthening Tax Policy**

- **RI1** was fully adequate to measure the impact of PA1 (increase excise tax on petroleum products) on progress toward the targeted outcome. Increases in revenue from the petroleum excise tax, as a percentage of GDP (which would normalize the nominal PHP value of the revenue), were expected to be principally due to the increase in the excise tax rate on petroleum products. The definition of the results indicator was clear; there was credible baseline data and a clear target; and credible data was available to measure the achievement of the target. This results indicator is rated satisfactory.

- **RI2** aimed to measure the impact of PA2 on progress toward achievement of the targeted outcome. The assumption with this indicator was that increases in revenue from the VAT, as a percentage of GDP (which would normalize the nominal PHP value of the revenue), would be due to the repeal of tax laws and rules granting non-essential VAT tax exemptions. The essential question, however, is whether the results indicator would measure only the increase in the VAT revenue that was attributable to the reduction of the VAT tax breaks. The ICR (pages 12-13) offers an alternative measure that was drawn by the Department of Finance – "incremental VAT revenue from adjustments in VAT exemptions," which, while left undefined in the ICR, was later clarified to mean "the additional revenue from the reform each year if a VAT exemption for a good or service were removed, based on the quantity consumed of that good or service." However, this indicator (introduced after project completion) is that it did not have a target. As the ICR admits, "the [original] results indicator could have been formulated so as to more accurately clarify attribution to Prior Action 2." This results indicator is rated moderately satisfactory.

**Relevance of Results Indicators for Pillar 2 - Enhancing Public Financial Management and Budget Planning**

- **RI3** (was fully adequate to measure the impact of PA3 on progress toward the targeted outcome. The definition of the results indicator was clear, and credible data was available. Since the Department of Budget and Management directed that payments exceeding PHP 1 million be processed through the BTMS, the results indicator would be confined only to payments exceeding PHP 1 million (US$20,000), consistent with the circular. This results indicator is rated satisfactory.
- **RI4** aimed to measure the impact of PA4 on progress toward the targeted outcome. The definition of the results indicator was clear; there was credible baseline data and a clear target; and credible data was available. The results indicator was defined as the disbursement rate on the budget approved by Congress; a high disbursement rate would signify a low deviation between the approved budget and the executed budget. The assumption was that the one-year cash appropriation system would raise the disbursement rate on the approved budget. However, any improvement in the disbursement rate could not be solely driven by a changeover from obligation-based to cash-based budgeting. There could arguably be other factors, including more efficient budget execution by government agencies. For this reason, this results indicator is rated moderately unsatisfactory.

**Relevance of Results Indicators for Pillar 3 - Strengthening Fiscal Risk Management of Public Assets**

- **RI5** was fully adequate to measure the impact of PA5 on progress the targeted outcome. The assumption was that the creation of the National Asset Registry and the establishment of an indemnity insurance program would allow government agencies to record government assets in an official public registry, and enable them to have the assets insured against disaster risks. The definition of the results indicator was clear, and credible data is available. This results indicator is rated satisfactory

| Results Indicator | Relevance Rating | Efficacy Rating (from RI or Complementary Evidence) | Pillar Efficacy Rating | Overall Efficacy Rating |
|---|---|---|---|---|
| **Pillar 1: Strengthening Tax Policy** | | | | Satisfactory |
| RI1 | Satisfactory | High | Satisfactory | |
| RI2 | Moderately Satisfactory | Substantial | | |
| **Pillar 2: Enhancing Public Financial Management and Budget Planning** | | | | |
| RI3 | Satisfactory | High | Moderately Satisfactory | |
| RI4 | Moderately Unsatisfactory | Modest | | |
| **Pillar 3: Enhancing Fiscal Risk Management of Public Assets** | | | | |
| RI5 | Satisfactory | Substantial | Satisfactory | |

### Rating

Moderately Satisfactory

## 5. Achievement of Objectives (Efficacy)

## OBJECTIVE 1

### Objective

To strengthen tax policy.

### Rationale

The program exceeded the first target to strengthen tax policy, and nearly achieved the second.

- Revenue from the petroleum excise tax increased from 0.2 percent of GDP in 2017 to 0.7 percent of GDP in 2019, exceeding the target of 0.5 percent of GDP. TRAIN adjusted the excise taxes rates on 14 petroleum products in 2018 and made additional changes in 2019 and 2020. The increase in revenue from petroleum products drove the increase in overall tax revenue, which rose from 13.6 percent of GDP in 2017 to 14.5 percent of GDP in 2019 . Achievement of RI1 is rated High.
- Revenue from the VAT increased from 4.3 percent of GDP in 2017 to an estimated 4.5 percent of GDP in 2019, missing the target for an increase to 4.6 percent of TRAIN introduced several changes to the VAT: (a) a total of 54 exemptions pertaining to eight beneficiary sectors were repealed, broadening the tax base; and (b) the remaining exemptions, which were designed to protect the poor and the vulnerable, were expanded The reform raised the turnover threshold for exemption from VAT for companies, from PHP 2 million to PHP 3 million, and prescribed an accelerated processing of VAT refund applications, setting the target at 90 days from the filing of an application. According to the ICR (pages 11-13), incremental VAT revenues as a result of the tax exemption reform was 0.045 percent of GDP from 2017 to 2019. Meanwhile, total VAT revenue rose from PHP 706 billion in 2017 to PHL

833 billion in 2019. Hence, the reform of VAT exemptions would account for only 6.7 percent of the increase in VAT collections over two years. Achievement of RI2 is rated Substantial.

### Rating

Satisfactory

## OBJECTIVE 2

### Objective

To enhance public finance management and budget planning.

### Rationale

The program achieved the outcome targets to enhance public financial management and budget planning.

- The share of payments processed through the BTMS increased from zero in 2017 to 30 percent in 2019, exceeding the target that at least 10 percent of payments, by value, be processed through the BTMS. The Secretary of the Department of Budget Management issued a circular letter in January 2019 requiring all national government agencies to use the BTMS for high-value transactions (transactions of PHP 1 million or more) by July 1, 2019. These transactions represented only 5 percent of the total number of transactions in 2018 but approximately 30 percent of expenditures by all spending units, in terms of value, in 2019. These transactions were executed through the TSA. Achievement of RI3 is rated High.
- The Department of Budget and Management and the Bureau of the Treasury were the first oversight agencies to use the BTMS, while other agencies, including the Department of Public Works and Highways and the Department of Trade and Industry, started preparations for the adoption of BTMS in 2018. BTMS covers the execution and utilization phases of the budget cycle and supports public financial management functions It provides standard workflows and signing authorities for the budget utilization process, generating standard forms, documents and reports in digital form and producing comprehensive financial reports, at the consolidated and agency levels and at the disaggregated level, which cover financial statements, standard and custom reports, and planning and performance management reports. The decision to cover high-value transactions at all national government agencies in the BTMS accelerated the deployment of the BTMS in 2019.
- The disbursement rate on the annual budget (actual disbursements, as a share of total funds in the annual budget approved by Congress) improved from 68.5 percent in 2017 to 79.9 percent in 2018 and 84 percent in 2019, exceeding the target of 80 percent by 2019. The proposal for a cash-based budget planning and management system was initially resisted by Congress. A draft Budget Modernization Law with provisions for cash-based budgeting and other reforms was submitted to Congress in 2018 but was not passed. That decision led to the re-enactment of the 2018 budget instead for the first four months of 2019. The amended 2019 budget was subsequently approved by the Congress in February 2019 and, while it confirmed the introduction of cash-based appropriations, the legislation provided for a one-year obligation limit for appropriations as a transitional arrangement. The President's veto message in April 2019 asserted that a cash-based budget for 2019 would be mandated nevertheless; this arrangement would ensure the availability of cash resources for priority development projects. However, because of the delayed passage of the 2019 budget and the conduct of national and local elections in May 2019, authorization was given only for the

implementation and payment of infrastructure projects until the end of 2020 (provided that the funds for these projects were obligated no later than the end of 2019).

The target for the results indicator (RI4) associated with the prior action was met – the disbursement rate on the FY 2019 budget was 84 percent, above the 80 percent target – but the one-year cash-based national budgeting system was yet to be fully implemented. there is an issue of results attribution with this indicator. According to the ICR (pages 14-15), other factors may have driven the improvement in the disbursement rate. Reforms were under way over several years to reduce the under-utilization of appropriations: (a) the validity period for obligations was reduced; and (b) the monitoring and review of allocations and expenditures was intensified. The ICR also states that while the government remains committed to changing the long-established obligation-based system that has persisted for more than 30 years, the transition to a cash-based budgeting system will likely require several years of institutional learning and adjustment. Given the poor relevance of the indicator, achievement is rated Modest

### Rating

Moderately Satisfactory

## OBJECTIVE 3

### Objective

To strengthen fiscal risk management of public assets.

### Rationale

The program achieved the outcome target to strengthen fiscal risk management of public assets.

- Five government agencies had submitted their list of their assets to the public asset registry by December 2019, meeting the target that at least five departments / agencies will have their asset data included in the National Asset Registry by end-2019. Achievement of RI5 is rated Substantial.
- To establish the institutional framework for the financial risk management of public assets against disasters, the government: (a) created a new Asset Registry Division under the Bureau of the Treasury; (b) designated the Bureau of the Treasury as the agency in charge of managing the Public Asset Registry; and (c) issued Development Budget Coordination Committee Resolution No. 2019-4 establishing a Working Group, comprised of the Office of the President and the key oversight agencies, that would adopt a common policy on the management of national government non-financial assets and set the groundwork for a permanent governmental body on asset management. To develop instruments that insure key assets, the government provided budgetary funding in the General Appropriations Act of 2019 for: (a) the National Disaster Risk Reduction and Management Fund; (b) the public asset indemnity insurance program; (c) a public asset insurance program that would reduce the government's contingent liability and ensure that sufficient resources were available for the reconstruction of public assets. The budgetary provision would allow the renewal and expansion of the parametric catastrophe risk insurance program that would provide liquidity to government agencies and 25 provinces in response to severe events.

**Rating**

Satisfactory

### Overall Achievement of Objectives (Efficacy)
### Rationale

The program exceeded the first and nearly achieved the second target for objective to strengthen tax policy. The program achieved the two targets for the objective to enhance public financial management and budget planning, but there were attribution issues with the second outcome. The program achieved the target for the objective to strengthen fiscal risk management of public assets. Overall, the degree of achievement of the program objectives is rated Satisfactory.

### Overall Efficacy Rating
Satisfactory

## 6. Outcome

### Rationale

The program objectives were relevant to the development challenges faced by the Philippines in raising public spending on capital investment and human development: the prior actions to increase the excise taxes on petroleum products and to eliminate non-essential exemptions to the VAT were relevant to boosting tax revenues, thereby increasing the fiscal space for public investment and more inclusive social spending; the prior actions to introduce cash-based budgeting and a centralized budget and treasury management system were relevant to address weaknesses in public financial management; and the prior action to strengthen the risk management of public assets was relevant to address regular losses incurred by the government as a result of natural disasters. The targets associated with the four out of the five outcome indicators were achieved, while the fifth – incremental VAT revenue as a result of tax exemption reform – fell only slightly short of the target. There was an attribution issue with improvement in the budgetary disbursement rate because the shift to a cash-based budgeting system, on which the result was associated, was not fully implemented. Overall, the shortcomings were minor, and the operation's outcome is rated Satisfactory.

### a. Rating

Satisfactory

## 7. Risk to Development Outcome

**Political Risk.** Past uncertain support in Congress for the one-year cash appropriation system poses political risks to the sustainability of the development outcome of this operation.  Because the cash budgeting system had been adopted by an amendment to the annual appropriation act for 2019, and with caveats rather than through a more enduring Budget Modernization Law as originally proposed, it remains plausible that the reform could be reversed or weakened by future annual appropriation acts.

**Policy Risk.** The executive branch provided stronger policy support for the reforms than the legislature. According to the ICR (page 20), the strength of the dialogue "provides an assurance of policy consistency and ownership of the reform objectives, not only of the oversight agencies, but also of the line agencies executing the reforms on the ground," helping mitigate the risks to the development outcomes of this operation. In response, the Bank has prepared a programmatic series of three development policy operations to maintain momentum for the reforms. The first in the series, which aims to promote competitiveness and enhance resilience to natural disasters, was approved by the Board in December 2019, and included prior actions and triggers related to tax policy, public financial management and budget planning, and public asset management. The second was approved in December 2020, and the third is slated for approval in December 2021.

**Institutional Capacity Risk.**  As cited by the Project Document, weak institutional capacity adds to the risks to the sustainability of the development outcomes of this program.  Complex inter-government relations and, sometimes overlapping mandates across public agencies present challenges for effective implementation. In addition, implementation capacity has frequently been compromised by fragmentation in the bureaucracy, a dearth of managerial staff, weak managerial information systems, a lack of performance incentives for the civil service, and corruption.

**Macroeconomic Risk.**  According to the Bank's *East Asia (EAP) and Pacific Economic Update – Uneven Recovery* of April 2021, the Philippines economy contracted the most and will likely recover the slowest among ten developing economies in the Region in 2020 (excluding the Pacific Island economies). GDP shrank 9.5 percent in 2020, and output is not expected to return to the level attained in the fourth quarter of 2019 until the third quarter of 2022. The slow recovery should convince policymakers of the added urgency of fiscal reforms to support economic growth. On the other hand, it could give politicians another argument to postpone reforms, on the premise that difficult measures would exact a toll on public welfare.

**COVID-19 Risk.** The Philippines reported the strictest lockdown (average daily score of 66 on Oxford University's Stringency Index, where 100 = strictest) in the EAP region (median average daily score of 50 on the index), but recorded the highest COVID-19 deaths per million (84 deaths per million) in the region (median of 4 deaths per million). It has also conducted the second-to-lowest number of tests per confirmed COVID-19 case (17) in the region (median of 113 per million), and has so far delivered only 1.46 million vaccinations in mid-April 2021 to a population of 109.6 million.  Limited success with the health response would heighten the risk of a slower economic recovery, and hence exacerbate the risk of greater political and public resistance to difficult reform measures.

## 8. Assessment of Bank Performance

### a. Bank Performance – Design

#### Rationale

**Lessons from Experience.** Program design was informed by extensive analytic work produced by, or with the assistance of, the Bank and other development partners:

- assessments, studies, and reports related to tax reform, public financial management, and fiscal risk management of public assets – 10 of these analytic products are listed in Section 3.B, and include, *the PEFA Assessment* (2016)*,* the *Public Investment Management Assessment* (IMF and World Bank, 2018), and the *Financial Protection Against Natural Disasters: An Operational Framework for Disaster Risk Financing and Insurance* (2014);
- analytic and advisory services delivered through the Game Changers for Inclusive Growth Program (P159649 related to tax policy and tax administration reform, including on the CTRP, TRAIN, changes in excise taxes, and VAT tax reform; and,
- a simulation of the distributional effects of the CTRP using the EPIQ structural macro model.

The reforms supported by this program were aligned with related Bank operations in the Philippines preceding or following this program:

- The Disaster Risk Management Development Policy Loan with a Catastrophe-Deferred Drawdown Option (Cat-DDO) approved in 2011, and the Second Disaster Risk Management Development Policy Loan with a Catastrophe-Deferred Drawdown Option approved in 2015, aimed to enhance the capacity of the government to mitigate disaster risk and manage the socio-economic and fiscal impacts of natural disasters.
- The Social Welfare and Development Reform Project approved in 2009, aimed to strengthen the effectiveness of the social protection agency to efficiently implement the Conditional Cash Transfer Program, the *Pantawid Pamilyang Pilipino* Program, and the National Household Targeting System for social protection programs, and the Second Social Welfare and Development Reform Project approved in 2016, aimed to support the Conditional Cash Transfer program to improve the use of health and education services by poor children.

**Risk Identification and Mitigation.** The Program Document (pages 41-42) rated two of nine operational risks to the project as substantial, and recommended mitigation measures.

- Political and governance risks were substantial and would be mitigated by: choosing reform objectives and targets that had a high degree of government ownership; intensifying the dialogue with the economic team of the government; and continuously assessing the degree of support for the reform program.
- Institutional capacity risks were substantial and would be mitigated by: technical assistance and operational support to the supervising and implementing agencies; continuous policy dialogue among government agencies themselves; and transparency measures at government agencies to better anchor the reform objectives.
- An important shortcoming at the design stage is that the Bank appears not to have completely vetted the risks related to legislative action on the shift from an obligation-based to a one-year cash-based national budget system. The proposed Budget Modernization Law providing for a cash-based budgeting system was not passed by Congress.

**Stakeholder Consultation.** The Bank and the government conducted consultations about the program with stakeholders using: (a) public meetings on the Philippine Development Plan for 2017-22, with which the program objectives were aligned. These involved extensive discussions nation-wide, organized around thematic clusters, with various stakeholders; and (b) consultative meetings of the Philippine Development Forum, the principal mechanism by which the government engages civil society, academe, the private sector, and legislative representatives in dialogue on the country's development agenda. These involved discussions about the program objectives and results target in 2017 and 2018.

**Development Partners Coordination.** The ICR (page 19) reports that the Bank consulted many development partners on the design of the program: (a) on tax policy and administration reform –IMF, ADB, and the Australian Department of Foreign Affairs and Trade; (b) on public financial management and budget reform – IMF, ADB, the UNDP, European Union, USAid, JICA, Agence Française de Développement, and the Australian Department of Foreign Affairs and Trade; and (c) on disaster risk finance management – the ADB and JICA..

### Rating

Moderately Satisfactory

### b. Bank Performance – Implementation

### Rationale

**Monitoring.** The government reported comprehensive data and information updates to the Bank.

**Adaptation.** As this was a stand-alone operation, there were no issues with triggers (prior actions to the next series in the program) made necessary by changed circumstances and priorities. The ICR (page 21), however, reported that the Bank had prepared a three-part programmatic development policy operation to succeed this program with at least six prior actions related to this program: (a) directive for all national government agencies to adopt the BTMS for all transactions above PHP 1 million; (b) creation of a body to formulate and recommend public asset management policies; (c) implementation of a risk-layering strategy by setting financial instruments to meet the funding needs of disasters; (d) an increase in excise taxes (this time, on alcohol and e-cigarette products); (e) operationalization of the indemnity insurance of public assets; and (f) the adoption of an asset management policy to improve financial risk management derived from natural disasters and climate change. The prior actions and triggers of the new series are linked to the prior actions and development objectives of this program.

### Rating

Satisfactory

### c. Overall Bank Performance

### Rationale

The Bank's performance on program design is rated moderately satisfactory. The Bank drew on extensive analytic and advisory work on tax policy, public financial management and budget planning, and the fiscal risk management of public assets to prepare this program. The Bank ensured that consultations were conducted with stakeholders and with development partners. The Bank, however, appears not to have fully vetted the risks related to legislative action on the cash-based national budget system. The Bank's performance on program implementation is rated satisfactory. The program was properly monitored, and the Bank linked the reforms supported by this operation with the objectives of succeeding development policy operations. Overall, the Bank's performance is rated satisfactory.

### Overall Bank Performance Rating

Satisfactory

## 9. Other Impacts

### a. Social and Poverty

The Program Appraisal Document (pages 35-38) explained that  the reforms supported by this program were expected to have positive poverty and social impacts.

- On Strengthening Tax Policy. The increase in the excise taxes on petroleum products and the repeal of VAT tax exemptions would reduce the after-tax income of all households. The impact would be 1.3 percent of household income, on average, across all households, and 1.4 percent of household income for the poorest quintile.  To mitigate these effects, the government would deploy an Unconditional Cash Transfer program as well as transport subsidies for poorer households
- On Enhancing Public Financial Management and Budget Planning. The budget planning and execution reforms would benefit the poor by improving the effectiveness and transparency of government spending in areas benefitting poorer households, particularly agriculture, education, and public works.
- On Strengthening Fiscal Risk Management of Public Assets. The protection of public assets from natural disaster risks would benefit the poor and vulnerable. Recent studies of the economic and human losses from typhoons (tropical cyclones) in the Philippines showed that: (a) the average short-run effect of typhoons was to depress incomes by 6.7 percent, net of public and private transfers; (b) the income losses translated nearly one-for-one into reductions of household expenditures, decreasing the average household expenditure by 7.1 percent in the average year; (c) households did not mitigate storm-induced losses through consumption-smoothing strategies (in-kind transfers, savings, or borrowing) but instead by making large adjustments to their relative spending on different types of consumption and investment, reducing their spending on human capital investments (medicine, education, and high nutrient foods); (d) typhoons caused infant mortality to rise the calendar year after the storm itself had passed as a result of these reductions in household spending; annual average deaths reached 1,130 female infant deaths per million households, corresponding to 55 percent of the baseline infant female mortality rate.

The ICR (pages 17-18) provided some evidence of these social and poverty impacts.

- On Strengthening Tax Policy. The Unconditional Cash Transfer program had become the single largest social mitigation measure under TRAIN. Cash grants were provided to poor households and indigent senior citizens who did not directly benefit from lower personal income tax rates but were adversely affected by higher prices due to excise taxes and the repeal of VAT tax exemptions. In 2018, some PHP 22.29 million was allocated to 9,288,993 households. In 2019-20, another PHP 18.44 billion was released to 5,122,276 households. The cash grants amounted to PHP 200 per month in 2018, and PHP 300 per month in 2019-20.
- A study by the Bank in 2019, using the structural macro model EPIQ, concluded that the Unconditional Cash Transfer program led to a substantial reduction in poverty. The poverty rate, measured as the share of population living on less than US$3.20 per day, dropped from 24.7 percent in the baseline to 23.3 percent in 2020 under TRAIN. Although the Unconditional Cash Transfer program would end in 2021, the poverty rate would decrease by an additional 0.6 percentage points in 2021-30, compared to the baseline.
- On Enhancing Public Financial Management and Budget Planning and on Strengthening Fiscal Risk Management of Public Assets. Measures related to public financial management and the risk management of public assets were not expected to directly impact the distribution of incomes. However, indirect effects could occur. More efficient public financial management and a more strategic response to fiscal risks from natural disasters would, in principle, free up government resources for social spending.

### b. Environmental

The Program Appraisal Document (pages 38-39) stated that the reforms supported by this program were expected to have positive environmental impacts.

- On Strengthening Fiscal Risk Management of Public Assets. With the reforms, improved information on assets owned by the government would allow faster damage assessments and pre-agreed rehabilitation plans and , insurance mechanisms would unlock funds for the rehabilitation of key infrastructure assets and public buildings.

The ICR (page 18) added to the discussion of the environmental impacts but presented no additional evidence.

- On Strengthening Tax Policy. The increase in the excise taxes on petroleum products would likely reduce the use of fuel and have a positive impact on environmental pollution. The ICR did not quantify this effect.
- On Strengthening Fiscal Risk Management of Public Assets. The acquisition and publication of data on public assets would help promote risk-informed development planning by the government. Budgetary procedures for public asset rehabilitation (in the event of natural disasters) would ensure that sufficient funding was allocated for reconstruction work, and that the standards for reconstruction work required under environmental impact assessments were dutifully met.

### c. Gender

According to the Program Document (page 38), it was not suitable to "gender-tag" this tax policy, public financial management, and fiscal risk reform operation.

### d. Other

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## 10. Quality of ICR

### Rationale

The ICR ably explained the context for the reform measures supported by this operation: (a) the macroeconomic setting and the justification for policy priorities placed on tax revenue mobilization, public financial management, and the management of fiscal risks to public assets; (b) the relationship of the prior actions to the wider program for policy reform in these areas; and (c) the relationship of this operation to other Bank programs in closely related policy areas, including succeeding development policy operations.

The assessment of the results indicators was candid. Despite the contribution of tax exemption reform to incremental VAT revenues, the growth in general economic activity still accounted for the larger part of gains in VAT revenues over two years. The ICR contends that the results indicator could have been formulated "so as to more accurately clarify attribution [of the result] to Prior Action 2."

The assessment of the program outcomes was equally candid. The program achieved the target for the disbursement rate on the national budget, but the government has yet to fully implement the one-year cash-based national budgeting system, on which the result was predicated. Clearly, other reform measures, pursued outside the purview of this program, had driven the higher budgetary disbursement rate. The ICR lists several possible explanations, based on evidence about related reform measures that were implemented by the government before this operation.

### a. Rating

Substantial

## 11. Ratings

| Ratings | ICR | IEG | Reason for Disagreement/Comments |
|---|---|---|---|
| Outcome | Satisfactory | Satisfactory | |
| Bank Performance | Satisfactory | Satisfactory | |
| Relevance of Results Indicators | --- | Moderately Satisfactory | |

| | | |
|---|---|---|
| Quality of ICR | --- | Substantial |

## 12. Lessons

Two lessons are drawn from the ICR (pages 20-21), with some adaptation.

**Prior actions that require legislative action are subject to considerable risk, owing to complex political dynamics in legislatures.** A proposed Budget Modernization Law providing for a shift from an obligation-based to a one-year cash-based national budget was not approved by the bicameral legislature. Compensating measures could not fully implement a cash-based national budget: (a) the final budget for 2019 adopted an obligation-based budget with a one-year obligation limit, ostensibly as a transitional arrangement; and (b) the Presidential veto mandated a cash-based budget but could only apply the system to infrastructure projects until the end of 2020. The ICR admits that it will likely take time to shift from the three-decade-old obligation-based budget to a cash-based budget.

**Knowledge products and technical assistance are vital to designing complex reforms.** Extensive analytical work on tax policy helped design the Comprehensive Tax Reform Program for the Philippines, stage the tax reform process over a six-part legislative package, and choose the prior actions supported by this operation – the increase in excise taxes for petroleum products and the repeal of non-essential exemptions to the VAT. Analytical and advisory services were also helpful in preparing the Unconditional Cash Transfer program supported by this operation as a social amelioration measure to help mitigate the impact of tax reform on poor households. The knowledge-based work also helped sustain the momentum for reforms in a new development policy loan series succeeding this operation.

## 13. Project Performance Assessment Report (PPAR) Recommended?

No