Sustainable Capacity Building for Small Water Utilities

Improving Small Water Utilities and Financing Technical Assistance: Lessons from the Philippines

November 2015

INTRODUCTION

The Philippines has surpassed its Millennium Development Goals (MDGs) for safe water supply, with 92% of households now able to access water. By 2025, the Philippine government plans to achieve universal coverage and more equitably distributed service outside of the capital. However, serving the “last mile”—households that are often remote or very poor—will be extremely challenging. There are about 4,700 water utilities providing piped water connection, seventy-one percent of which are small and currently not regulated.¹ Strengthening the capacity and performance of these water utilities will be critical in achieving universal access to water.

To help small water utilities reach the remaining unserved population, the World Bank’s Water and Sanitation Program (WSP)—a multi-donor partnership that is part of the World Bank Group’s Water Global Practice—and the National Water Resources Board (NWRB) launched an initiative in 2010 called the Accreditation of Technical Services Providers Program. The accreditation program connects small water utilities with technical experts through a reliable and sustainable system that has produced encouraging results.

This learning note explains the key interventions carried out in the past five years and examines the implementation challenges, results, and important lessons learned. This learning note provides insights for scaling the program and challenges that need to be addressed for it to become a sustainable solution for small water utilities in the Philippines.

¹ Estimates of the number of utilities were derived from the initial results of the Listahang Tubig (as of July 2015), a national survey of water utilities in the Philippines, led by the National Water Resources Board and supported by the World Bank’s Water and Sanitation Program.
PROBLEM STATEMENT
Small water utilities play an important role in the Philippines by filling gaps where medium and large utilities do not operate, ultimately serving 30% of piped water consumers or about 13 million Filipinos. These small utilities have fewer than 5,000 connections each and represent about half of the country’s water utilities. Most of these utilities came about with the decentralization of water supply services to local government units. With the decentralization, the government handed responsibilities to local authorities, but due to limited technical knowledge and lack of funds the local governments struggled to back further development of water utilities.

Without outside support, small water utilities were unable to build capacity or raise sufficient funds to expand and improve their businesses. Banks offered few solutions as their loan terms were incompatible with utilities’ needs, and utilities lacked experience preparing project proposals to appeal to loan officers. Additionally, many small utilities were unregistered and unknown to the government’s water regulator, further isolating utilities from potential assistance. Some water utilities received sporadic, project-based capacity building, but could not count on continuous support. They showed little promise of reaching the remaining eight million Filipinos without access to improved water sources.

In 2010, NWRB and WSP stepped in to foster sustainable capacity-building opportunities in the highly fragmented market for business development services. The overall strategy was to build an industry around the water sector where technical experts could gain training and accreditation, and where utilities could easily connect with water regulators and a pool of technical experts. This approach aimed to address both the demand and supply sides of the market for technical assistance. Since capacity building services were limited, a key component of the initiative involved recruitment, training, and certification of the experts who would serve the water utilities. The ultimate goal of the intervention was to boost water utilities’ management, operating capacity, and performance and regulatory compliance standards (Figure 1).
ACTION
WSP and NWRB designed a comprehensive technical assistance package to primarily support the water utilities, with technical experts and regulators as secondary beneficiaries. The four key components included:

1) **Training and accreditation of providers.** This component, led by NWRB, provided training and certification to technical experts who could provide consistent, high quality consulting services to water utilities (Figure 2). The training included sessions on the latest regulatory processes and requirements to promote compliance among utilities. A website facilitated the accreditation process for consultants and helped water utilities connect with certified consultants.

2) **Establishment of a standard package of consultancy services.** The program team developed a basic set of consultancy services and a pricing structure to standardize offerings for: general support, institutional development, regulatory compliance, and technical and financial services. The team also developed and provided toolkits and methodologies to the consultants. Within this framework, most standard services could be provided to water utilities within 10 days at a cost of US$1,200 for one consultant, with actual travel costs billed separately. The consulting services were made available to any of the 4,700 water utilities in the country with a focus on small, rural utilities that showed interest in receiving assistance. Tools and methodologies offered in the package of services included:

   - Preparation of documents for obtaining an operating license
   - Regulatory compliance for tariff setting or adjustment (applying the regulator’s five-year tariff methodology)
   - Business plans, operations manuals, and customer service codes
   - Measures to improve operational and financial efficiency (financial management controls, meter reading, billing, and collection)
   - Pre-feasibility studies for expansion and application of financing.

3) **Creation of a revolving fund.** Since some water utilities are not able to pay for consulting services on a lump sum basis, a revolving fund was created to expand utilities’ financing options. Through the fund, water utilities could take one-year loans to cover consultants’ fees and travel costs with a minimal processing fee of 2% or about US$50.

![Figure 2: Illustration of Types of Consultants Working with Utilities](image-url)
4) **Promotion and partnership.** This component aimed to increase participation of water utilities in the program, to create connections with technical experts within the water sector, and to motivate actors to improve performance and regulatory compliance. Marketing campaigns promoted the benefits of the offering, and stressed the importance of regulatory compliance. The accredited experts led the majority of the promotion efforts, but complementary strategies included referrals by water utilities and NWRB, outreach to private sector partners and a federation of industry associations, and advertisements.

**PROGRAM RESULTS**

At the end of 2014, the program had met or exceeded all its original targets for accreditation of experts, provision of technical assistance, and delivery of services (Figure 3). Participating water utilities enjoyed significant gains, as did regulators and technical experts.

**Increased Demand for Technical Expertise**

Seventy-eight experts received training and accreditation to provide technical, financial, and/or institutional consulting services. Twenty-three percent of accredited experts provided technical assistance to 61 water utilities, and marketing efforts actively promoted the program’s services to additional water utilities. Technical experts enjoyed an increase in demand for services, and are well positioned to receive larger contracts with water utilities in the future.

**Improved Utility Performance**

The technical assistance for preparation of strategic business plans, and review and adjustment of the tariff structure provided the water utilities with transparent management and governance tools. Water utilities were guided in the use of a systematic and logical framework in reviewing operations, setting targets, identifying corrective measures and deciding on investment programs. The technical assistance has contributed to investment decisions for new household connections and other capital expenditures contributing to operating efficiency. Although modest, there were improvements in the performance indicators of assisted water utilities, as seen in Table 1.

**Increased Regulatory Compliance**

The program has significantly increased the number of water utilities complying with regulatory requirements. As of February 2015, 22 of the 61 assisted water utilities had applied for licenses to operate, eight applications had been approved, and the rest were still being processed. The economic regulator also observed that the quality of applicants’ business plans improved significantly, increasing the rate at which tariff proposals could be approved—from 4 months to 2 months in some cases.

**Table 1. Financial and Operational Performance of Assisted Water Utilities**

<table>
<thead>
<tr>
<th>Performance Indicator</th>
<th>No. of Utilities</th>
<th>Pre-Assistance</th>
<th>2013</th>
<th>Change</th>
<th>% Change</th>
</tr>
</thead>
<tbody>
<tr>
<td>Average Cost/m³ Sold</td>
<td>11</td>
<td>14.07</td>
<td>13.89</td>
<td>-0.18</td>
<td>-1%</td>
</tr>
<tr>
<td># Staff/1000 Connections</td>
<td>14</td>
<td>8.2</td>
<td>7.7</td>
<td>-0.5</td>
<td>-6%</td>
</tr>
<tr>
<td>Non-Revenue Water</td>
<td>15</td>
<td>30%</td>
<td>25%</td>
<td>-6%</td>
<td>-6%</td>
</tr>
</tbody>
</table>

www.wsp.org
Lesson 1: The private sector can play a supportive role in helping the regulator operate more efficiently and effectively.

The technical assistance and regulatory tools, such as business planning, performance improvement plans, and tariff models based on the NWRB five-year methodology, helped water utilities comply with regulatory requirements. As a result, NWRB has been able to carry out its regulatory functions more effectively and efficiently. Accredited experts should continue to promote their services as these efforts have helped increase the awareness of many utilities about NWRB’s regulatory functions and requirements, as well as the advantages of being regulated and the repercussion of not being regulated.

Lesson 2: Building a market for business development services is more sustainable and cost-efficient at scale than direct technical assistance to water utilities.

A comparison of the cost and benefit of the accreditation program versus project-based capacity building activities conducted by WSP from 2007 to 2010 shows that investment in the program is more cost efficient and has the potential to achieve higher returns. The program has significantly lower capacity development costs per utility, and although cost per capita was higher for the pilot, it is on track to drop well below that of project-based interventions as the program reaches scale in the next five years. The program is also more sustainable and responsive to water utilities’ needs compared to project-based efforts, as assistance is on demand and largely self-financed by water utilities.

Lesson 3: The current technical assistance package is not sufficient to facilitate water utilities’ access to finance.

The current technical assistance packages may not be enough to enable water utilities to borrow from lending institutions. However, the outputs of the assistance provide critical information for credit analysis, which is an important first step. Looking ahead, NWRB can gain insights from the six cases in which water utilities applied for loans using their business plans to back

Modestly Improved Access to Finance

The initiative improved some utilities’ capacity to leverage internal and external financing. With better performance and financial management, water utilities generated enough cash internally to fund nearly US$3 million in new investments. A portion of the new investments came from loans, which became more accessible to utilities with guidance from the program.

Broader Water Service Coverage

Participating water utilities improved and expanded their services to more customers. A comparison of the service coverage of 22 utilities before (2011) and after the program (2013), indicated an increase from 50% to 53%. A total of 43,779 more people (7,851 households) were provided with piped water service (Figure 4), of which 43% were poor.

LESSON LEARNED

The first few years of the initiative have not only shown encouraging results, but have also highlighted opportunities for further improvement. As NWRB plans to scale the program to more than 500 small water utilities—roughly 25% nationwide—over the next 4 years, the following are important to consider:
the applications. Four utilities successfully obtained loans from commercial banks, a private investor, and a social lending institution.

**Lesson 4: Sustaining government commitment is key to scaling up the program.**
The cost-effectiveness and initial success of the initiative provide compelling reasons to scale up the effort to reach all unregulated utilities. This will require strong government commitment, including resource allocation. Fortunately, NWRB has taken the necessary steps to institutionalize the program, including securing Board approval of the Accreditation Guidelines, creation of the Accreditation Committee and including an allocation to expand the program in its current budget request.

**Lesson 5: There is market opportunity to scale the initiative.**
The current needs of water utilities and the growing demand for water supply services will require additional support for expansion and improvement of operations. NWRB is planning to conduct training workshops to accredit about 30 technical experts annually in the regions outside Metro Manila over the next five years. The training sessions are envisioned to meet the technical assistance requirements of 525 target water utilities, including those operating in areas with high incidence of poverty and lowest coverage. Previous expansion projects from assisted water utilities have averaged 952 new people connected per utility. This means that about 500,000 more people will gain access to improved water supply.

**Lesson 6: Consultant selection is critical but challenging.**
Recruiting top-notch consultants and setting reasonable fees for their services proved to be challenging. Recruiters tapped top consulting firms, professional groups, companies assisting water utilities, and water districts to find talented candidates. Most recruits could command high fees, so making the consulting fees attractive to them while balancing the financial limitations of the small water utilities was difficult. This may well be the reason why only a quarter of the accredited consultants went on to provide technical assistance. Consultants who provided services to water utilities were motivated by a steady flow of assignments and potential opportunities for larger contracts in the future. Once a small pool of consultants bought into the program, their testimonials attracted more consultants to be accredited. To encourage participation of more accredited consultants, sustained demand for services is critical. In this regard, NWRB should actively promote the program to water utilities, expand its technical assistance coverage and allocate sufficient resources to the revolving fund.

![Figure 5: Participants in the Accreditation Workshop held in Baguio City, Philippines, April 2014](image-url)
RECOMMENDATIONS FOR ACHIEVING SCALE

New opportunities and challenges should be factored in by NWRB in scaling up the program.

1. **Target high-impact municipalities.** At inception, the program team focused on marketing to small private water utilities to address supply gaps in poor communities. However, for greater impact, the expansion should reach the 455 identified “waterless municipalities” defined by government as municipalities with less than 50% of their respective population with access to improved water supply. These municipalities are eligible for capital grants up to a point where their service coverage reaches 50%, beyond which water utilities raise their own capital financing. Expert services can thus focus on two objectives: to improve management capability to sustain the benefits of the grants, and to capacitate them to expand the service and access financing.

2. **Strengthen the revolving fund.** The revolving fund is an effective mechanism for encouraging water utilities to contract technical experts. To scale the program and allow more utilities to take out loans, the fund will require a higher balance. Funding sources can include budget appropriation, donor contribution or even possibly commercial funding, and the fund can also benefit from improved administration systems to enhance collection efficiency. It is also important for the fund to consider the needs of small water utilities, as initial participants in the program are now generating more project proposals for funding. They may benefit from a lending facility for their special needs, such as longer term loans, lower interest rates and leniency on the collateral.

3. **Get consultants closer to their clients in regions outside Metro Manila.** Gaining geographic coverage will require accreditation of a cadre of

Figure 6: Water Utility Planning

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consultants from across the country, or at least facilitation of travel for urban-based experts. As initial recruitment has shown, attracting top-notch expertise is important but challenging, so there needs to be a plan for attracting the best talent within each region and for determining how to fill gaps if no experts are available in certain areas. Also, the program should adjust technical assistance fees based on what is feasible for water utilities in different regions.

4. **Expand accreditation topics for experts to reflect new financing opportunities for water utilities.** The Philippine government is currently formulating a unified financing framework for the water supply sector with targeted financing programs for different market segments. Accredited expert services—and relatedly the current training program for experts—should be expanded to inform water utilities on any new financing opportunities, such as a loan/grant mix using output-based aid mechanisms, enhanced credit financing from local financing institutions or public private partnership (PPP) arrangements. Additional topics may also include credit discipline required by commercial financing entities, business case development, and transaction advisory services for PPP arrangements.

5. **Track and share the impact of the program with participating and target water utilities to maintain and grow participation.** NWRB can establish a management information system that can help track the impact of the expert services, which can then be marketed. Benchmarking of performance indicators, including health indicators will be integral to such an effort. Moreover, NWRB can facilitate customer satisfaction surveys to generate insights into community perceptions and to identify gaps and areas for improvement.

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**About the Program**

The Accredited Technical Service Provider Program is one of three components of the Expanded Small Water Utilities Improvement and Financing Technical Assistance that seeks to develop and implement new sector approaches—“light-handed” regulation, technical support to small utilities on a fee-basis by accredited service providers, and access to finance—to promote systematic acceleration of water service provision in unserved areas. The Program is being implemented by the National Water Resources Board with technical support from WSP. For more information, please visit http://www7.denr.gov.ph/NWRBAccreditationSystem/

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