

**AMENDMENT TO THE LOAN AGREEMENT BETWEEN THE DEVELOPMENT BANK
OF THE PHILIPPINES AND THE BANK
FOR THE LOCAL GOVERNMENT UNITS (LGU)
URBAN WATER AND SANITATION PROJECT-PHASE II (LOAN 7080-PH)**

1. The Project is the second phase of the Republic of the Philippines Program of Local Government Units (LGU) Urban Water and Sanitation Development. The Program aims to attract private sector management expertise to help LGUs and Water Districts operate water supply systems in a sustainable manner. Once a robust track record of cash flow generation from operating these systems is established, the Program is expected to generate private financing to the sector. The Program objectives have therefore both a medium and long-term aspect.
2. **Project Objectives** - The objective of the Project is to assist selected LGUs and Water Districts to: (a) provide sustainable water and sanitation services; and (b) strengthen their institutional and technical capacity for planning, budgeting and financial management of local services, including water supply and sanitation. The Project comprises two parts: (a) improvement of water supply, sanitation, and drainage services in selected LGUs and Water Districts through the financing of investment projects to construct, rehabilitate and expand water supply systems, on-site sanitation facilities and micro-drainage infrastructure; and (b) strengthening the capacity of selected LGUs, Water Districts and the Borrower for investment planning and financial management, supervision of construction, supervision of environmental management, and monitoring and evaluation, through the provision of consultant services, training and equipment.
3. The Project is financed by a Loan of JPY 3,717,900,000 (roughly US\$ 30.0 equivalent) for civil works, and associated water and sanitation systems, and consultant services. The Loan was approved by the Bank on November 19, 2001, and amended on February 24, 2003 to include credit-worthy water districts as participating entities. On May 28, 2004, the Loan was amended for the second time to include new categories and changes in the procurement schedule. The closing date of the Loan is November 30, 2006.
4. This is the first partial cancellation of the loan and modification of the Project Performance Indicators requested by the Borrower. The proposed amendment will not change either the Project Development Objectives or the project design. However, the outcome indicator of the water supply component will be reduced significantly from 60 to 11 participating LGUs, and the output indicator from 40 to 5 water supply systems successfully constructed with lease and management contracts. While the reduction in the Loan is significant, the participating LGUs are larger than anticipated in the Project Appraisal Document, and allocation of funds per LGU has increased substantially for the water supply component. Also, at present there is no demand from LGUs for the sanitation component, and this component is unlikely to be used. Therefore the indicator for measuring the sanitation component was lowered from 50% to 10%. As the overall number of LGUs participating in the Project will be reduced, and the number of transactions expected to have disputes requiring resolution is lower than the original number anticipated in the PAD, the indicator of conflict resolution was reduced from 70 % to 35%. Other indicators are unchanged.
5. The revision of the Project Performance Indicators - now incorporated as Schedule 7 to the Loan Agreement as proposed by the Borrower does not require either a reappraisal of the Project, or a new action plan. The revised Project Performance Indicators (Schedule 7 to the Loan Agreement) are attached to this memo.

6. **Implementation Progress** - Project implementation has been very slow due to the low demand from the LGUs and Water Districts because of the availability of funds from other more recent donor financed projects, with better terms compared to the Bank Program. These new projects offer a similar type of financing at a lower overall cost to the LGUs. Some new projects do not charge commitment fees and have longer loan maturity periods. Originally, around 40 LGUs took advantage of the PHRD Grant for preparing the feasibility studies and procurement documents for inclusion in the Project. The project preparation and implementation have assisted in the development of a healthy pipeline of sub-projects consistent with its development objectives. However, with the availability of cheaper financing from other projects, most of the LGUs have migrated to the new, non-Bank projects for financing of these sub-projects. The issue of more harmonized financing of local development projects has now been taken up through a Government-Development Partners Working Group on Decentralization and Local Government.

7. Twelve water supply systems are under different phases of implementation in the LGUs of: Tabuk, Lopez Jaena, Calamba, Castilla, San Mariano, Sigma, San Fernando City, San Gabriel, Bacnotan, San Juan, Bauang, and Santo Nino. Implementation is substantially completed in three LGUs; construction is underway in three LGUs; and in the remaining cases, bids are expected to be received in August 2005. In addition, the Nasugbu Water District has just signed the Subsidiary Loan Agreement with the Development Bank of the Philippines (DBP), and bids for this water district are expected in September 2005. An application from Santa Cruz, an LGU in Davao Province, is being processed by DBP.

8. Performance of the Borrower has been marginally unsatisfactory, mostly due to procurement delays and less than satisfactory financial management. LGUs have, in general, substantially delayed the evaluation of proposals, mainly because of weak capacity to deal with Bank procurement. The financial management problem is mainly caused by delays in providing Project Management Reports (which is a semi-annual report due 45 days after the end of each semester) to the Bank. However, the 2003 audited financial statements of the project were submitted to the Bank on December 13, 2004. The auditors rendered an unqualified opinion on the 2003 project financial statements. On May 25, 2005, the Bank received the Project Management Reports of May 2003, November 2003, May 2004, and November 2004.

9. Despite the difficulties in project implementation, LGUs and Water Districts included in the Project are expected to fully implement the water system and operate them in a sustainable manner. The Project is viable and can achieve its objectives, even with the reduced number of LGUs.

10. Although the number of LGUs and Water Districts included in the project will be reduced, the participating LGUs and Water Districts will benefit fully from the project. However, the full impact of the Project in the Program cannot be assessed at this time. Continued support to the LGUs is consistent with the new Country Assistance Strategy, which emphasizes the establishment of a comprehensive LGU platform.

SCHEDULE 7

Revised Project Performance Indicators

Project Development Objective:	Outcome / Impact Indicators:	Project reports:	(from Objective to Purpose)
<p>1. Consumers in approximately 11 participating LGUs are provided with clean and sustainable water supply.</p>	<p>1. CAU/Regulatory body resolves conflicts between LGUs/customers and Operators without resort to contract cancellations in at least 35% of PSP contracts.</p> <p>2. Water production per connection in all systems meets the design parameters.</p> <p>3. At least 10% of households without sanitation offers improve sanitation services.</p> <p>4. Average of 80% of consumers satisfied with service performance in participating LGUs</p> <p>5. Performance in LGUs with constructed systems.</p> <p>6. Low income consumers living within service area receive house connections</p>	<p>Technical Working Committee (DOF, DBP and DILG) monitors and evaluate success in implementing subprojects with assistance from DBP-PMO and DILG WSS- PMO:</p> <p>1. Biannual Review of CAU/Regulatory Body functioning.</p> <p>2. Evaluation of service performance in project towns compared to sample of non-participating towns.</p> <p>3. Assessments of Consumer Satisfaction in participating towns through household surveys, public performance audits.</p> <p>4. Program mid-term Reviews.</p>	<p>1. Successor LGU administrations will remain committed to maintaining agreements with regard to tariffs and honoring long-term contracts with the private sector for operations and maintenance</p>
Output from each component:	Output Indicators:	Project reports:	(from Outputs to Objective)
<p>1. Water supply systems are successfully constructed in project towns.</p>	<p>1. At least 5 additional towns with lease and management contracts by the end of APL2.</p>	<p>DBP-PMO and WSS-PMO through:</p> <p>1. Monitoring disputes in lease and management contract implementation.</p> <p>2. Monthly report of construction Supervision Consultant.</p> <p>3. Environmental indicator monitoring.</p>	<p>1. Newly elected LGU administrations will remain committed to agreements between the project and communities;</p>

OFFICE MEMORANDUM

DATE: June 2, 2005

TO: Mr. Jemal ud-din Kassum, Vice President, EAP

THROUGH: Keshav Varma, Sector Director, EASUR

FROM: Luiz Tavares, Task Team Leader

EXTENSION: 30597

SUBJECT: Philippines: Local Government Units (LGU) Water and Sanitation Project APL2 (Loan 7080-PH)--Request for Amendment to the Loan Agreement

1. We received a letter dated March 31, 2005 from the Department of Finance (DOF, the Guarantor), and a letter from the Development Bank of the Philippines (DBP, the Borrower), dated December 23, 2004, requesting a partial cancellation of the Loan in the amount of JPY 1,858, 950,000 (around US\$15 million, or 50% of the Loan) and revision of the Project Performance Indicators. These letters are attached to this memo.

2. The Country Director has determined (in consultation with the Task Team and LEGEA) that the proposed changes in the scope of the Project are significant, as a result of the proposed partial loan cancellation. According to BP 13.05, significant changes in the Project need to be submitted to the Board for approval. In the task team's judgment, the revised Project Performance Indicators, which originally were provided for in a supplemental letter and now are incorporated into the Loan Agreement as Schedule 7, will require Board approval on a no-objection basis.

3. The project is the second phase of the Republic of the Philippines Program of Local Government Units (LGU) Urban Water and Sanitation Development. The Program aims to attract private sector management expertise to help LGUs and Water Districts operate water supply systems in a sustainable manner. Once a robust track record of cash flow generation from operating these systems is established, the Program is expected to generate private financing to the sector. The Program objectives have therefore both a medium and long-term aspect.

4. The objective of the Project is to assist selected LGUs and Water Districts to: (a) provide sustainable water and sanitation services; and (b) strengthen their institutional and technical capacity for planning, budgeting and financial management of local services, including water supply and sanitation. The Project comprises two parts: (a) improvement of water supply, sanitation, and drainage services in selected LGUs and Water Districts through the financing of investment projects to construct, rehabilitate and expand water supply systems, on-site sanitation facilities and micro-drainage infrastructure; and (b) strengthening the capacity of selected LGUs, Water Districts and the Borrower for investment planning and financial management, supervision of

construction, supervision of environmental management, and monitoring and evaluation, through the provision of consultant services, training and equipment.

5. The Project is financed by a Loan of JPY 3,717,900,000 for civil works, and associated water and sanitation systems, and consultant services. The Loan was approved by the Bank on November 19, 2001, and amended on February 24, 2003 to include credit-worthy water districts as participating entities. On May 28, 2004, the Loan was amended for the second time to include new categories and changes in the procurement schedule. The closing date of the Loan is November 30, 2006.

6. This is the first partial cancellation of the loan and modification of the Project Performance Indicators requested by the Borrower. The proposed amendment will not change either the Project Development Objectives or the project design. However, the outcome indicator of the water supply component will be reduced significantly from 60 to 11 participating LGUs, and the output indicator from 40 to 5 additional water supply systems with lease and management contracts. While the reduction in the Loan is significant, the participating LGUs are larger than anticipated in the PAD, and allocation of funds per LGU has increased substantially for the water supply component. Also, at present there is no demand from LGUs for the sanitation component, and this component is unlikely to be used. Therefore, the indicator for measuring the sanitation component was lowered from 50% to 10% of households having improved sanitation services. As the overall number of LGUs participating in the Project will be reduced, and the number of transactions expected to have disputes requiring resolution is lower than the original number anticipated in the PAD, the indicator of conflict resolution was reduced from 70 % to 35%.

7. The revision of the Project Performance Indicators - now incorporated as Schedule 7 to the Loan Agreement as proposed by the Borrower does not require either a reappraisal of the Project, or a new action plan. The revised Project Performance Indicators (Schedule 7 to the Loan Agreement) are attached to this memo.

Implementation Progress

8. Project implementation has been very slow due to the low demand from the LGUs and Water Districts because of the availability of funds from other more recent donor financed projects, with better terms compared to the Bank Program. These new projects, some housed in DBP, and others in the Land Bank of the Philippines, offer a similar type of financing at a lower overall cost to the LGUs. Some of the funds from other donors do not charge commitment fees and have longer loan maturity periods. Originally, around 40 LGUs took advantage of the PHRD Grant for preparing the feasibility studies and procurement documents for inclusion in the Project. However, with the availability of cheaper financing from other projects, most of the LGUs have migrated to the new, non-Bank financing.

9. Twelve water supply systems are under different phases of implementation in the LGUs of: Tabuk, Lopez Jaena, Calamba, Castilla, San Mariano, Sigma, San Fernando

City, San Gabriel, Bacnotan, San Juan, Bauang, and Sto Nino. Implementation is substantially completed in three LGUs; construction is underway in three LGUs; and in the remaining cases, bids are expected to be received in August 2005. In addition, the Nasugbu Water District has just signed the Subsidiary Loan Agreement with DBP, and bids for this water district are expected in September 2005. An application from Sta Cruz, an LGU in Davo Province, is being processed by DBP.

10. Performance of the Borrower has been marginally unsatisfactory, mostly due to procurement delays and less than satisfactory financial management. LGUs have, in general, substantially delayed the evaluation of proposals, mainly because of weak capacity to deal with Bank procurement. The financial management problem is mainly caused by delays in providing PMRs (which is a semi-annual report due 45 days after the end of each semester) to the Bank. However, the 2003 audited financial statements of the project were submitted to the Bank on December 13, 2004. The auditors rendered an unqualified opinion on the 2003 project financial statements. On May 25, 2005, the Bank received the PMRs of May 2003, November 2003, May 2004, and November 2004.

11. Despite the difficulties in project implementation, LGUs and Water Districts included in the Project are expected to fully implement the water system and operate them in a sustainable manner. The Project is viable and can achieve its objectives, even with the reduced number of LGUs.

Recommendation

12. Although the number of LGUs and Water Districts included in the project will be reduced, the participating LGUs and Water Districts will benefit fully from the project. However, the full impact of the Project in the Program cannot be assessed at this time. Continued support to the LGUs is consistent with the new CAS, which emphasizes the establishment of a comprehensive LGU platform.

13. I therefore recommend your concurrence with the Borrower's request and seek Board approval for the amendment to the project performance indicators that have been incorporated as Schedule 7 to the Loan Agreement, on a no objection basis. LEGEA and LOAG1 have cleared the amendment requested by the Borrower.

Attachments

Cleared with and cc: Ms. Mei Wang (LEGEA) and Mr. Hung Kim Phung (LOAG1)

cc: Messrs/Mmes. von Amsberg, Tumaliwan-Belizario, Azarcon, Hoban (EACPF); Zhang, Tavares (EASUR); Rey (EAPCO); Toft (LEGEA); Hume (EACPQ); IRIS4

The World Bank

INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT
INTERNATIONAL DEVELOPMENT ASSOCIATION

1818 H Street N.W.
Washington, D.C. 20433
U.S.A.

(202) 477-1234
Cable Address: INTBAFRAD
Cable Address: INDEVAS

_____, 2005

Honorable Cesar A. V. Purisima
Secretary
Department of Finance
DOF Bldg., BSP Complex
Roxas Blvd. Manila

Mr. Reynaldo G. David
President and Chief Executive Officer
Development Bank of the Philippines
Sen. Gil Puyat Avenue
Makati City, Manila

**Re: LGU Urban Water and Sanitation Project – Phase II (LN 7080-PH)
Amendments to the Loan Agreement**

Dear Secretary Purisima and Mr. David:

I refer to the Loan Agreement dated November 19, 2001, between the International Bank for Reconstruction and Development (the Bank) and the Development Bank of the Philippines (the Borrower), as amended (the Loan Agreement) and the Guarantee Agreement between the Republic of the Philippines (the Guarantor) and the Bank for the above-referenced Project (the Project). I also refer to the letter dated December 23, 2004 from Mr. Reynaldo G. David representing the Borrower, and the letter dated March 31, 2005 from Mr. Roberto Tan representing the Guarantor, requesting the Bank to amend the Project performance indicators as a result of a partial loan cancellation.

I am pleased to inform you that after due consideration, the Bank agrees to amend the Project performance indicators. As you know, the Project performance indicators were originally provided for a supplemental letter dated November 19, 2001, signed by the Borrower and countersigned by the Bank and the Guarantor. To facilitate the amendments, we incorporated the revised Project performance indicators into the Loan Agreement as Schedule 7 to the Loan Agreement, which is attached to this letter.

Please confirm your agreement to the amendments set out in the attachment by having authorized representatives of the Borrower and Guarantor sign the form of confirmation set forth below, and returning one fully executed original of this amendment letter to us and retaining originals of the letter for your records.

This amendment letter shall become effective as of the date first above written, once it has been fully executed by all parties thereto.

Except as specifically amended by this amendment letter, all other provisions of the Loan Agreement otherwise remain in full force and effect.

Sincerely yours,

INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT

Joachim von Amsberg
Country Director, Philippines
East Asia and Pacific Region

CONFIRMED:
REPUBLIC OF THE PHILIPPINES

By _____
Authorized Representative
Name: _____
Title: _____
Date: _____

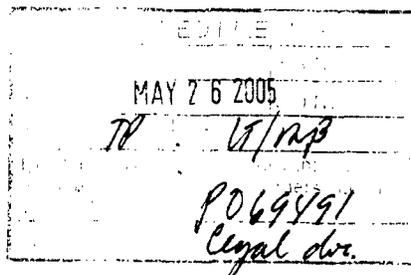
DEVELOPMENT BANK OF THE PHILIPPINES

By _____
Authorized Representative
Name: _____
Title: _____
Date: _____

May 25, 2005

Hon. Cesar V. Purisima
Secretary
Department of Finance
DOF Bldg., BSP Complex
Roxas Blvd., Manila

Mr. Reynaldo G. David
President and Chief Executive Officer
Development Bank of the Philippines
Sen. Gil Puyat Avenue
Makati City, Metro Manila



**Re: Philippines Local Government Units (LGU) Urban Water and
Sanitation Project Phase 2 (Loan Number 7080-PH)
Request for Partial Cancellation of Loan Amount**

I refer to the Loan Agreement for the Philippines Local Government Units (LGU) Urban Water and Sanitation Project Phase 2 between the International Bank for Reconstruction and Development (the Bank) and the Development Bank of the Philippines (the Borrower), dated November 19, 2001 and the Guarantee Agreement between the Republic of the Philippines and the Bank of the same date. I also refer to the letter of the Borrower dated December 23, 2004 and the letter dated March 31, 2005 from Mr. Roberto B. Tan, Assistant Secretary of the Department of Finance (DOF), requesting a partial cancellation in the amount of JPY 1,858, 950,000 (US\$ 15 million equivalent) from the Loan for the purpose of reducing commitment charges being paid by the Borrower to the Bank.

Pursuant to section 6.03 of the General Conditions, the Bank hereby cancels, as of April 1, 2005, the amount of JPY 1,858, 950,000 from the Loan, and the commitment charges on such amount cease to accrue from April 1, 2005.

The amortization schedule is being revised by the Bank as a result of the cancellation, and the revised figures will be sent to you shortly. Attached please find the revised table in paragraph 1 of Schedule 1 to the Loan Agreement.

Sincerely,

Joachim von Amsberg
Country Director, Philippines
East Asia and Pacific Region

Attachment: as stated

Attachment

1. The table below sets forth the Categories of items to be financed out of the proceeds of the Loan, the allocation of the amounts of the Loan to each Category and the percentage of expenditures for items so to be financed in each Category:

<u>Category</u>	<u>Amount of the Loan Allocated (Expressed in Yen)</u>	<u>% of Expenditures to be Financed</u>
1. Works, including supply and installation of water and sanitation system		90%
(A) Type A Sub-projects and Type C Sub-projects	1,200,000,000	
(B) Type B Sub-projects		
	173,144,440	
2. Consultants' services under Parts A and B of the Project	198,288,000	100%
	250,338,600	Amount due pursuant to Section 2.02 (b) of LA
3. Interest accrued on or before 31 July 2006		Amount due under Section 2.04 of LA
4. Fee	37,179,000	
5. Goods	0	100% of foreign expenditures, 100% of local expenditures (ex- factory cost) and 90% of local expenditures for other items procured locally
TOTAL	<u>1,858,950,000</u>	
Cancellation as of April 1, 2005	1,858,950,000	
Original Loan Amount	3,717,900,000	

Hon. Cesar V. Purisima
Mr. Reynaldo G. David

- 3 -

May 25, 2005

Prepared by and Bcc: L. Tavares (EASUR)

Cleared with and Bcc: M. Wang (LEGEA); H. K. Phung (LOAG1); K. Varma (EASUR)

Bcc: Messrs/Mmes. von Amsberg, Tumaliwan-Belizario, Azarcon, Hoban (EACPF); Zhang, Tavares (EASUR); Rey (EAPCO); Toft (LEGEA); Hume (EACPQ); IRIS4



Republic of the Philippines
DEPARTMENT OF FINANCE

Roxas Boulevard Corner Pablo Ocampo, Sr. Street
Manila 1004

31 March 2005

MR. JOACHIM VON AMSBERG
Country Director, Philippines
The World Bank - RMP
23rd Floor, The Taipan Place
Emerald Avenue, Ortigas Center
Pasig City

Accession No.	Doc. No.
FPN	APR - 1 2005
Act	RA/TP
Project	LT/LA/RB/IB/ET
Project No.	PO69491
Project Name	Legal doc.

Dear **Mr. Amsberg**:

Reference is made to the request of the Development Bank of the Philippines (DBP) and endorsement by the National Economic and Development Authority (NEDA) for partial loan cancellation in the amount of US\$ 15 million or JPY 1,858,950,000.00 from the IBRD funded LGU Urban Water and Sanitation Project - Phase II (Loan 7080-PH).

The Department of Finance favorably endorses the request for partial loan cancellation in order to reduce the commitment fees DBP is paying to the World Bank. The table below shows the allocation of the loan after the partial loan cancellation:

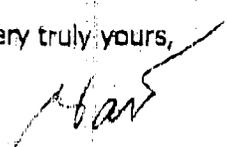
Category	Loan Allocation (Expressed in Yen)	Proposed Cancellation (Expressed in Yen)	Proposed Allocation (Expressed in Yen)	% of Expenditures to be financed
1. Works and goods	2,968,123,500	1,594,979,100	1,373,144,400	90%
2. Consultant's services under Parts A and B of the project	204,484,500	6,196,500	198,288,000	100%
3. Interest accrued on or before 31 July 2006	508,113,000	257,774,400	250,338,600	Amounts due pursuant to Section 2.02 (b) of LA
4. Fee	37,179,000	0	37,179,000	Amounts due under Section 2.04 of LA
Total	3,717,900,000	1,858,950,000	1,858,950,000	

As a result of the proposed partial loan cancellation, the Project Design Summary is likewise recommended for amendment. Committed and pipeline projects due for completion by loan closing date under the project are now implemented only in 11 participating LGUs and only 10 towns have lease and management contracts with PSP-led operators.

Project Development Objectives (minutes of negotiations)	Proposed Project Development Objective
Consumers in approximately 60 participating LGUs are with clean and sustainable water supply and sanitation services.	Consumers in approximately 11 participating LGUs are with clean and sustainable water supply.
Program Purpose	Proposed Program Purpose
Phase II (APL 2): Based on the lessons learned from APL 1, adjusting and modifying the project design and applying it to about 40 LGUs and other government agencies in order to create a sufficiently large market to attract a PSP-led water operators industry.	Phase II (APL 2): Based on the lessons learned from APL 1, adjusting and modifying the project design and applying it to about 11 LGUs and other government agencies in order to create a sufficiently large market to attract a PSP-led water operators industry.
Key Performance Indicators	Proposed Key Performance Indicators
At least 30 additional towns with lease and management contracts by end of APL 2.	At least 10 additional towns with lease and management contracts by end of APL 2.

We shall look forward to the Bank's usual cooperation and prompt action.
Best regards.

Very truly yours,


ROBERTO B. TAN
Assistant Secretary



Copy for: Case History 1400

Republic of the Philippines
NATIONAL ECONOMIC AND DEVELOPMENT AUTHORITY

NEDA sa Pasig, 12 Blessed Josemaria Escrivá Drive, Ortigas Center, Pasig City 1605
P.O. Box 419, Greenhills • Tels. 631-0945 to 64
<http://www.neda.gov.ph>

11 March 2005

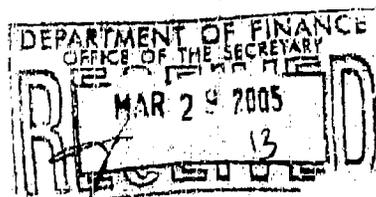
Honorable Cesar V. Purisima
Secretary
Department of Finance
6th Floor, Executive Tower Building
BSP Complex, Roxas Boulevard
Manila 1004

Dear Secretary Purisima:

This refers to your letter dated 10 January 2005 seeking NEDA's position on the request of the Development Bank of the Philippines (DBP) for the cancellation of US\$15.0 million under the World Bank-assisted LGU-Urban Water Supply and Sanitation Project (LGU-UWSP) APL 2.

In order to save on commitment fees, we are endorsing the request for partial loan cancellation in the amount of US\$15.0 million or JPY 1,858,950,000.00 from the following categories of the above-mentioned project: (a) Works and Goods, (b) Consultant's Services under Part A and B, and (c) Interest accrued on or before 31 July 2006. Accordingly, the allocation per category would be as follows:

Category	Loan Allocation (Expressed in Yen)	Proposed Cancellation (Expressed in Yen)	Proposed Allocation (Expressed in Yen)	% of Expenditures to be Financed
1. Works and goods	2,968,123,500	1,594,979,100	1,373,144,400	90%
2. Consultant's services under Part B of the Project	204,484,500	6,196,500	198,288,000	100%
3. Interest accrued on or before 31 July 2006	508,113,000	257,774,400	250,338,600	Amounts due pursuant to Section 2.02 (b) of LA.
4. Fee	37,179,000	0	37,179,000	Amounts due under Section 2.04 of LA
Total	3,717,900,000	1,858,950,000	1,858,950,000	



Category	Loan Allocation (Expressed in US Dollar)	Proposed Cancellation (Expressed in US Dollar)	Proposed Allocation (Expressed in US Dollar)	% of Expenditures to be Financed
1. Works and goods	23,950,000	12,870,000	11,080,000	90%
2. Consultant's services under Part B of the Project	1,650,000	50,000	1,600,000	100%
3. Interest accrued on or before 31 July 2006	4,100,000	2,080,000	2,020,000	Amounts due pursuant to Section 2.02 (b) of LA
4. Fee	300,000	0	300,000	Amount due under Section 2.04 of LA
Total	30,000,000	15,000,000	15,000,000	

Correspondingly, the Project Design Summary is likewise recommended for amendment as a result of the proposed partial loan cancellation. Committed and pipeline projects due for completion by loan closing date under the project are now implemented only in 11 participating LGUs and only ten (10) towns have lease and management contracts with PSP-led operators. Hence, the Project Design Summary should be amended as follows:

Project Development Objectives (minutes of negotiation)	Proposed Project Development Objective
Consumers in approximately 80 participating LGUs are with clean and sustainable water supply and sanitation services.	Consumers in approximately 11 participating LGUs are with clean and sustainable water supply.

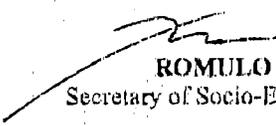
Program Purpose	Proposed Program Purpose
Phase II (APL 2): Based on the lessons learned from APL 1, adjusting and modifying the project design and applying it to about 40 LGUs and other government agencies in order to create a sufficiently large market to attract a PSP-led water operators industry.	Phase II (APL 2): Based on the lessons learned from APL 1, adjusting and modifying the project design and applying it to about 11 LGUs and other government agencies in order to create a sufficiently large market to attract a PSP-led water operators industry.

Key Performance Indicators	Proposed Key Performance Indicators
At least 30 additional towns with lease and management contracts by end of APL 2.	At least 10 additional towns with lease and management contracts by end of APL 2.

We would appreciate your immediate endorsement (copy furnished NEDA) of the same to World Bank.

Thank you and best regards.

Very truly yours,


ROMULO L. NERI
 Secretary of Socio-Economic Planning

Development Bank of the Philippines

Office of the President & CEO

December 23, 2004

HON. JUANITA D. AMATONG

Secretary
Department of Finance
6th Floor DOF Building
Roxas Blvd. Cor. Pablo Ocampo St.,
1004, Manila

Attention : **HON. ROBERTO B. TAN**
Asst. Secretary
International Finance Operation Office

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Donor-Aid Coord./Internal Affairs / Liaising/	Topical / Adm.
Folder / Sub-folder:	

Accession No. **DEC 29 2004**
Action **RM** cc **UT/IS/RA/113**
Folder / Sub-folder: **Legal**

Dear Secretary Amatong:

The loan Agreement of the LGU-UWSP APL 2 (Loan Number 7080 PH) JPY 3,717,900,000 or \$ 30,000,000 between the Development Bank of the Philippines (DBP) and International Bank for Reconstruction and Development (IBRD) was signed on November 19, 2001. The facility is the second phase of the LGU Urban Water Supply and Sanitation Project to finance forty (40) LGUs. The objective of the facility is to assist the selected LGUs to: (a) provide sustainable water and sanitation services and (b) strengthen their institutional and technical capacity for planning, budgeting and financial management of local services including the water supply and sanitation.

Among the Components of the project are as follows;

Components	World Bank Financing (US \$)
Water Supply/Works	19,160,000.00
Water Supply/Goods	4,790,000.00
Consultancy Services	1,650,000.00
Total Project Cost	25,600,000.00
Interest During Construction	4,100,000.00
Front End Fee	300,000.00
Total Financing Requirements	30,000,000.00

During the project level review held on August 12, 2004, we informed the World Bank delegation headed by Mr. Chris Hoban, that the projected disbursement up to the closing period, November 19, 2006, of the program is only \$13,420,000. We proposed the reduction of the facility from \$30,000,000.00 to \$15,000,000.00 to fund the pipeline projects with the exclusion of the specific component for sanitation and drainage in the eligible categories for financing in as much as we have no existing pipeline project for such component.

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Consequently, the Project Design Summary should also be amended as follows:

Project Development Objective (minutes of negotiations)	Proposed Project Development Objective
1. Consumers in approximately 60 participating LGUs are with clean and sustainable water supply and sanitation services.	Consumers in approximately 11 participating LGUs are with clean and sustainable water supply.

Program Purpose	Proposed Program Purpose
Phase 11 (APL 2): Based on the lessons learned from APL 1, adjusting and modifying the project design and applying it to about 40 LGUs and other government agencies in order to create a sufficiently large market to attract a PSP-led water operators industry.	Phase 11 (APL 2): Based on the lessons learned from APL 1, adjusting and modifying the project design and applying it to about 11 LGUs and other government agencies in order to create a sufficiently large market to attract a PSP-led water operators industry.

Key Performance Indicators	Proposed Key Performance Indicators
At least 30 additional towns with lease and management contracts by the end of APL 2	At least 10 additional towns with lease and management contracts by the end of APL 2

The number of LGUs to be financed under amended amount shall also be reduced from 40 LGUs to 11 LGUs. The Output Based Aide Project of the Province of La Union is counted as 5 LGUs corresponding to the five municipalities the project will serve.

In view thereof, we are recommending reduction of LGU UWSP APL 2 facility from \$ 30 million to \$ 15 million. The proposed reduction of the facility will consequently reduce the commitment fees DBP is paying to World Bank. Thus, we earnestly request for your immediate indorsement in order to save on commitment fees.

Thank you and kind regards.

Very truly yours,



REYNALDO G. DAVID

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MR. LUIZ TAVARES
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