



RESPONSE OF THE LEAGUE OF CITIES OF THE PHILIPPINES TO THE SECTORAL CONSULTATION ON FEDERALISM

Consistent with its commitment of leading a proactive local government, the League of Cities of the Philippines (League) is keen in exploring on how and what federalism can do to the local government units. The League has been very receptive to the ideas and propositions presented during national discourse, while not doing away with its duty to examine whether the same bring the greater good to the local government units and the country as a whole.

To accommodate the proposal to shift our system from unitary to federal, there must be a fundamental change in the 1987 Constitution. In several forum discussing initiatives for federalism, the League articulates¹ its view on the universal concept of federalism taking into consideration a number of proposals in the Philippine context, and how a federal form of government works on local governments. It focuses more on the General Provisions on Local Government provided for in Article X of the Constitution. Pending additional inputs and comments from the member-cities, the League is currently in the process of carefully reviewing the proposals.

Through the laudable efforts of the Local Government Foundation (LOGODEF) and other key proponents of federalism, the League puts forward its interest and concerns on prevailing propositions in relation to the discussion on decentralization and local governance, its issues and limitations.

I. Internal Revenue Allotment

The calculation of IRA, as it is today, is not adequately responsive to prevailing conditions such as urban population growth. In 1996, the IRA per capita for Philippine cities is 20% higher than that of provinces and municipalities. Based on the research conducted by the League in 2011, the IRA per capita of Philippine cities is 40% lower than the IRA per capita of provinces and municipalities. The IRA also lacks an equalizing feature resulting in disparities in the LGU's fiscal capabilities and, in turn, uneven economic development. IRA also tend to have a disincentive effect on local income generation for LGUs that are dependent on IRA.

¹ THE LEAGUE OF CITIES OF THE PHILIPPINES PROPOSITION ON FEDERALISM: The Local Government Perspective.
Annex A



The IRA is allocated as a block grant and, as such, LGUs enjoy discretion on how it will be used. It follows in principle that the intent of IRA is to encourage innovations in local governance. However, IRA is hardly keeping up with the rising cost of devolved functions, unfunded mandates, and population growth. Such inadequacy of the IRA stands as a challenge to LGUs that desire to introduce innovative programs in their respective jurisdictions. Naturally, the efficacy of policies and plans are assessed on the quality of their implementation, which substantially is dependent on available funding. In addition, the poor predictability in the size of the IRA undermines the ability of LGUs to effectively plan and manage their expenditures.

Reforms geared toward greater local autonomy should consider more of tax assignments than revenue sharing or grants, which based on Philippine experience tend to promote dependence of LGUs on the national government. Meanwhile, the improvement of the IRA system should focus on being more responsive to factors such as population growth, providing incentives for local tax effort, and better predictability for the purpose of planning.

II. Proposed Model of Federal Philippine Government

Shifting to a federal structure of government could be an initial step toward addressing some of the problems associated with the manner the Philippines have decentralized in the past two decades. For instance, local governments at the same nominal level vary considerably in their capacities. Put differently, not all cities (nor municipalities) are created equal.

The proposed model gives an opportunity to bridge such gap by institutionalizing representation of cities in particular in the Federal and Regional Assemblies and a closer access to funding than the current set up. In this regard, the proposed model empowers cities in the planning process and in accessing the funds to fuel the implementation of such plans. Moreover, it also promotes countryside development, especially cities, as they are constitutionally enabled to stand for the peculiar needs and interest of their jurisdictions.

The creation of several Regional Governments theoretically implies a stronger and more focused oversight since Regional Governments, under the proposed model, will be responsible in overseeing fewer local government units, compared to the current set up where such power and responsibility resides at the national level (e.g., DILG). Such proposed arrangement, in turn, will boost governance accountability.



III. Amendment and Thorough Implementation of the 1991 Local Government Code

If the Constitution will not be revised, the true intent of decentralization may still be furthered by introducing amendments to the 1991 Local Government Code and a more thorough implementation of the same.

If the reason behind efforts in decentralizing is to allow LGUs to manage their resources for countryside development, the LGC under Article 10 Section 5 already gives the LGUs the power to create its own sources of revenues and to levy taxes, fees and charges subject to such guidelines and limitations as Congress may provide. Further, Section 7 mandates an equitable share in the proceeds of the national wealth for the local governments. At the same time, however, amendments to the LGC are still needed such as improving the system for the Internal Revenue Allotment (IRA) with particular consideration to population as there is a considerable concentration of people in cities. Furthermore, existing cities may benefit from the institutionalization of Inter-LGU Cooperation in the LGC and specific amendments to the creation, conversion, and creation of LGUs.

The League, in several consultations with key stakeholders for the revision of the Local Government Code, manifested the following positions², to wit:

1. SECTION 17 OF THE LOCAL GOVERNMENT CODE ON BASIC SERVICES AND FACILITIES

To achieve greater clarity in functional assignment, it is proposed that Section 17 (a) of the 1991 LGC be amended by inserting a proviso that will differentiate fully devolved functions and shared functions.

Fully devolved functions are those for which exclusive responsibility for service provision is assigned to LGUs.

Shared functions are those which should be broken down into more specific competencies (e.g., health, agriculture, environment and natural resources, infrastructure) with National Government being responsible for some of the competencies and LGUs being responsible for other competencies

The amendment seeks to articulate the principles in delineating which functions should be assigned to NG (e.g. those associated with externalities) and which should be assigned to LGUs (e.g., those whose

² Official Position Paper of the League of Cities of the Philippines on Local Government Code Review. Annex B.



benefits are local in scope). It is acknowledged that the assignment of shared functions will have implications on financing. Let the IRR delineate the share of funding to be provided by NG and LGUs, respectively, based on criteria to be defined by NG and the LGUs.

The League believes that by clearly delineating which level of government should provide the services, it would result in a more efficient allocation of resources. LCP sees the value in delineating the functions as we have been strong advocates of performance-based grants. But for shared functions, these have to be further studied. Will capacity or need dictate which functions will be shared between national governments and local governments?

2. SECTION 143 OF THE LOCAL GOVERNMENT CODE ON THE LOCAL BUSINESS TAX.

The League supports the proposal to amend Section 143 by simplifying the differentiated and graduated local business tax structure that currently applies to different types of business enterprises to a single flat tax rate not exceeding 1.5% of their gross receipts/sales regardless of the type of business. The different graduated local business tax rate for different types of business complicates local tax administration for several reasons. First, the present graduated structure is regressive because it imposes higher effective tax rates on smaller businesses relative to larger ones. Second, the disparities in effective tax rates with respect to the size and type of business tend to provide a venue for tax evasion. Also, the revenue impact of this proposal is P36B pesos for cities.

The low local tax to GDP ratio of and low own source revenue to GDP ratio of all LGUs in the aggregate as well as their heavy reliance on the fiscal transfers, particularly the IRA is indicative of the low degree of revenue autonomy of the LGUs. As a result, it is predicted that accountability at the local level will continue to weaken.

One of the explanations for the inability of LGUs to fully maximized their taxing powers is that the LGC prescribes different tax rates for different categories of firms. This tends to increase the administrative and compliance costs.



3. SECTION 450 OF THE LOCAL GOVERNMENT CODE ON THE CONVERSION OR CREATION OF LGUS

The League supports the proposal to align income requirements for the creation/conversion of highly urbanized city, province and municipality with that in RA 9009 which provides new income criteria for the creation of cities.

The amendments introduced to the Local Government Code by piecemeal legislation should be integrated therein to exhaustively cover the system of laws pertaining to the local government units. In this case, the Code must reflect the most current applicable provisions to guide the creation and conversion of local government units.

A. Income Requirement of Highly Urbanized Cities

The League supports the proposal to increase the income requirement of HUCs to P 250 Million locally generated average annual income for the last two (2) consecutive years based on 2000 prices. Taking into consideration the amendment by RA 9009 which increases the income requirement for the conversion of a municipality to a component city, there is a cogent reason that the requirement for HUCs be revised. Logically, the increase classifies one city from the other. Consequently, the negative effects of conversion to the rest of the cities will be cured.

B. Conversion to Highly Urbanized Cities

The League proposes that through an act of Congress the provisions on HUCs be reviewed and revised setting forth stricter guidelines for the declaration of a Highly Urbanized Cities. There shall be some other indicators, aside from the income requirement, for a city to be declared as such. Before the city shall be declared by the President as an HUC, its capability of carrying out high level services in terms of education, health and/or agriculture, among others and as it may be deemed appropriate in the area of jurisdiction, must be guaranteed. In effect, this sets apart the characteristics and the nature of HUCs from other cities; and such gives the spirit and intent of LGU classification.