

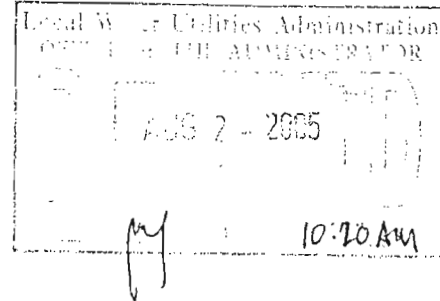


Republic of the Philippines  
**DEPARTMENT OF FINANCE**

Roxas Boulevard Corner Pablo Ocampo, Sr. Street  
Manila 1004

04 August 2005

**MR. LORENZO H. JAMORA**  
Administrator  
Local Water Utilities Administration  
Katipunan Road, Balara  
Quezon City



Dear Administrator Jamora:

We are pleased to transmit to your Office the attached Criteria for Classification of Water Districts (WDs) approved by the Oversight Committee last 21 July 2005. Said criteria shall be used by the Local Water Utilities Administration (LWUA) for categorization of WDs according to creditworthiness.

Thank you.

Very truly yours,

*Soledad Emilia J. Cruz*  
**SOLEDAD EMILIA J. CRUZ**  
Director IV  
Corporate Affairs Group

## CRITERIA FOR INITIAL CLASSIFICATION OF WATER DISTRICTS

### Objective:

The classification of water districts (WDs) and other water service providers (WSPs) is part of the financial reforms in the water sector mandated under Executive Order (EO) No. 279. The herein proposal evolved from the original study submitted by the Stone and Webster Consultants, and thereafter taken up and finalized by the Oversight Committee's Technical Working Group (TWG) composed of the Department of Finance (DOF), the Local Water Utilities Administration (LWUA) and the Government Financial Institutions (GFIs) (LBP and DBP).

The rationale of classifying the WDs and WSPs is to provide basis for rationalization allocation of financing for water supply systems/projects, which at present is limited or scarce. Under the reforms of the EO 279, the LWUA shall favor the non-creditworthy (NCW), pre-creditworthy (PCW) and semi-creditworthy WDs/WSPs. The government financing institutions (GFIs) and private financing institutions (PFIs) are now to be tapped as the primary source for financing the creditworthy WDs/WSPs. However, these WDs/WSPs may still apply for financing with LWUA but shall be accorded last priority in funds allocation.

Hereunder is the methodology in classifying WDs/WSPs:

1. A WDs/WSPs shall be classified as creditworthy, semi-creditworthy, pre-creditworthy using seven (7) parameters, namely:

- 1.a. Financial Parameters (50%)

- Current ratio
- Debt service ratio
- Debt equity ratio
- Net profit ratio


- 1.b. Operation Parameters (50%)

- Collection ratio
- Non-revenue water
- Staffing ratio

2. Procedure

- 2.1. Ratio computed for each parameter earns either 10, 6, 3 or 0 based on a given range for each parameter as indicated in the attached Annex 1.
  - 2.2. The earned points are multiplied by the assigned weight expressed in percentage for each ratio/parameter to get the weighted points.

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CAG Corporate Operations Office

- 2.3. The weighted points of all ratios are added to get the final points earned by WDs/WSPs.
- 2.4. The total weighted points of the WDs/WSPs shall determine its credit classification under the following category using the following ranges.

Creditworthy	8.5 – 10.0	points
Semi-creditworthy	5.5 – 8.4	
Pre-creditworthy	3.0 – 5.4	
Non-creditworthy	0.0 – 2.9	

- 2.5. Initial classification based on 2001 – 2003 financial statement (FS). A WD needs to maintain the classification under a particular category for three (3) consecutive years to be declared under that category.
- 2.6. The preceding procedure is summarized in Annex 1 table.
3. Below is the summary of the result of the Top forty-one (41) Borrowers' performance for the past three (3) years (2001 – 2003) which were validated under the recommended Classification Criteria. Details are presented in Annex II.

Total Number of Water Districts	Category	CW	SCW	PCW
3	VL	2	1	0
8	Large	1	6	1
14	Big	3	8	3
11	Medium	2	7	2
5	Average	2	1	2
0	Small	0	0	0
41		10	23	8

- 3.a.1 Water districts were earlier categorized into very large, large, big, medium, average and small, as approved by DBM in June 1997 (see Annex III). Pursuant to EO 279, WDs shall be classified into creditworthy, semi-creditworthy, pre-creditworthy and non-creditworthy.
- 3.a.2 For the period 2001 – 2003, the top forty-one (41) borrowers of LWUA used as samples for validating the classification criteria, proposals are:

Geographically distributed as follows:

Luzon: 20 WDs, Visayas: 8 WDs and Mindanao: 12 WDs

Distributed per LWUA's size categorization as follows:

Very Large: 3 *md*

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4. Below is the summary of the result of the fifty-one (51) medium sized water districts' performance for the past three (3) years (2001 – 2003) which were validated under the recommended Classification Criteria. Details are presented in Annex IV.

	51 Medium WDs	
	No. of WDs	%
Creditworthy	17	33%
Semi-creditworthy	29	57%
Pre-creditworthy	5	10%
Total	51	100%

Over-all, the recommended parameters, scores and weight assignments were found to reflect a reasonable picture of sampled WDs financial and operational strengths and weaknesses and therefore their capability to absorb less concessional financing conditions.

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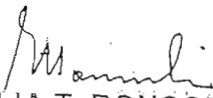
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Department of Finance  
Acting Secretary  
Chairman  
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National Economic & Development Authority  
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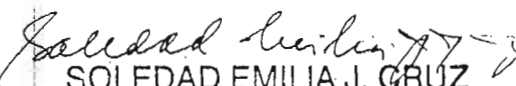
  
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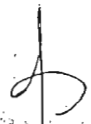
  
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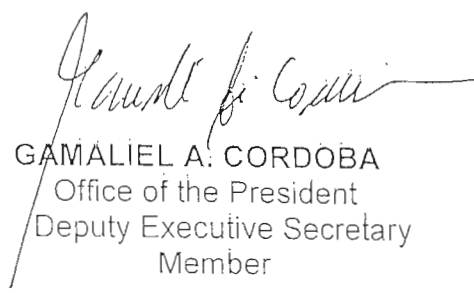
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CATEGORIZATION OF WATER DISTRICTS

1. For its objectives, the categorization aims to provide a basis for determining Organizational Structure/Staffing Pattern and Position Classification and Salary (initial categorization) and evaluate sustainability of operations under higher categories (recategorization allowed once every three (3) years.)
2. Initial Categorization
  - 2.a A water district will be *initially* categorized on the basis of total points earned, as follows:

Points Earned	Category
85 – 100	Very Large
70 – 84	Large
55 – 69	Big
40 – 54	Medium
25 – 39	Average
10 – 24	Small

- 2.b The parameters used are: a) gross receipts – 30%, b) number of personnel – 5%, c) number of service connections – 15%, d) nature of operation – 5%, e) total fixed assets – 25% and f) net income before depreciation and interests – 20%. Points are assigned for each range of values.

## 3. Recategorization

- 3.a Recategorization, which may be allowed once in three (3) years, uses the following financial and operational efficiency indicators. WDs need to hurdle the acceptable values as shown below:

Indicator	Acceptable Value	Definition
<b>Financial Efficiency</b>		
Operating ratio	Not more than 0.75	(O&M incld Dept. & int)/ Total Operating Revenue
Debt Service Coverage ratio	Not less than 2.0	
Current ratio	Not less than 1.5	
<b>Operational Efficiency</b>		
Unaccounted water	Not more than 40%	(Quantity Water Produced-Sold) / Water Produced
Staff Productivity Index	1 staff : 100 connections	Ratio of the number of personnel to the

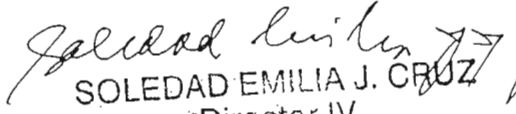
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Indicator	Acceptable Value	Definition
		number of Service connections

- 3.b Financial statements for the past two (2) years should show financial strength and stability using the above indicators. A three-year cash flow should also show full debt service coverage, minimum of 3% of gross receipts reserves and a cash balance at year-end of not-less than one-month total operating expense.

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CLASSIFICATION OF LWUA'S MEDUIM WDS  
Feb-05  
3-YEAR CLASSIFICATION (2001-2003)

	Creditworthy	Lowest in 3 yrs. Semireditworthy	Precreditworthy
	17	29	5
1	Binmaley	Alaminos	Norzagaray
2	Mangaldan	Ilocos Norte	Bago City
3	Tero Tuguegarao	La Trinidad	Talisay
4	Balanga	Manaoag	Calbayog City
5	Bulacan	Santiago City	Carigara
6	Dinalupihan	Urdaneta City	
7	Malolos	Bocaue	
8	Talavera	Guagua	
9	Lemery	Lubao	
10	Tanza	San Jose City	
11	Iriga City	San Miguel	
12	Dumangas Barotac-Nuevo	San Rafael	
13	Maasin	Subic	
14	San Francisco	Gen. Mariano Alvarez (GMA)	
15	Tandag	Pagsanjan	
16	Sultan Kudarat	Tanauan	
17	Dapitan City	Trece Martires	
18		Sorsogon	
19		Pili	
20		Daraga	
21		Gubat	
22		Virac	
23		La Carlota City	
24		Baybay	
25		Carcar	
26		Dumaguete City	
27		Naval	
28		Bislig	
29		Gen. Santos City	
	33%	57%	10%

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Total Weighted Score for Class	Creditworthy 8.5 - 10.0	Semi - CW 5.5 - 8.4			Pre - CW 3.0 - 5.4			Non - CW 0.00 - 2.9	Weight
		R	A	N	G	E			
Points	10 pts.	6 pts.			3 pts.			0 pts.	
<b>FINANCIAL:</b>									
Current Ratio (CR)	If CR > 2.0	If CR ≥ 1.2 but ≤ 2.0			If CR ≥ 0.9 but < 1.2			If CR < 0.9	20%
Debt Service Ratio (DSR)	If DSR > 2.3	If DSR ≥ 1.2 but ≤ 2.3			If DSR ≥ 0.9 but < 1.2			If DSR < 0.9	20%
Net Profit Ratio (NPR)	If NPR > 0.08	If NPR > 0.05 but ≤ 0.08			If NPR ≥ 0.03 but ≤ 0.05			If NPR < 0.03	5%
Debt Equity Ratio (DER)	If DER < 0.75	If DER ≥ 0.75 but ≤ 0.85			If DER > 0.85 but ≤ 1.0			If DER > 1.0	5%
<b>OPERATIONAL:</b>									
Collection Ratio (CR)	If CR ≥ 87%	If CR ≥ 78% < 87%			If CR ≥ 70% but < 78%			If CR < 70%	20%
Non-Revenue Water (NRW)	If NRW ≤ 25%	If NRW > 25% but ≤ 45%			If NRW > 45% BUT ≤ 55%			If NRW > 55%	20%
Service Conn./Staff (SR)	If SR ≥ 120	If SR ≥ 100 but < 120			If SR ≥ 80 but < 100			If SR < 80	10%
<b>T O T A L</b>									100%

Definition of Terms / Formula:

A. Financial

Current Ratio  
- Measures liquidity

Debt Service Ratio

Net Income before Interest + Depreciation / Debt Service (Int. + Principal)  
- Measures Solvency; Shows how many times debt service for a given period is covered by operations

Debt - Equity Ratio

Long Term Debt / Total Equity  
- Shows how much of the capital structure consists of debt, equity

Net Profit Ratio

Net Income / Total Revenue  
- Measures Profitability

B. Operational

Collection Ratio  
Collection of Current Year Water Sales + Collection of Accounts Receivables / (Total Billings, Water Sales + Average Accounts Receivable for the Year)

Non-Revenue Water

1 - (Volume Sold / Volume Produced)

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CLASSIFICATION OF SAMPLED TOP WD BORROWERS  
USING THE PROPOSED FINAL MODEL

2001		2002		2003		3-YEAR CLASSIFIC					
WD Categ.	Rate	WD Categ.	Rate	WD Categ.	Rate	WD Categ.	Rate				
<b>Creditworthy</b>											
17		16		15		10					
1	V-Large	Davao	9.20	V-Large	Davao	10.00	V-Large	Davao	9.20	V-Large	
2	V-Large	Quezon Metro	8.80	V-Large	Quezon Metro	8.80	V-Large	Quezon Metro	8.80	V-Large	Quezo
3	Large	Angeles City	9.20	Large	Angeles City	9.20	Large	Angeles City	9.20	Large	Ange
4	Large	Baquito	8.90	Large	Baquito City	9.20	Large	Metro Kalibo	9.00	Large	Suriga
5	Large	San Jose del Monte	8.80	Large	Metro Kalibo	9.20	Big	Surigao Metro	10.00	Big	Met
6	Big	Morong	10.00	Big	Surigao Metro	9.60	Big	Tarlac City	9.20	Big	
7	Big	Legazpi City	9.20	Big	Metro Naga	9.20	Big	Metro Naga	9.20	Medium	Ir
8	Big	Surigao Metro	9.60	Big	Tabaco	9.20	Big	Tabaco	9.20	Medium	Metro Tuc
9	Big	Metro Naga	9.20	Big	Morong	9.20	Big	Legazpi City	8.50	Average	
10	Big	San Pablo	9.10	Big	Butuan City	9.00	Medium	Daraqa	9.60	Average	
11	Big	Tabaco	8.60	Big	Cotabato City	9.00	Medium	Digos	9.60		
12	Medium	Iriga	10.00	Medium	Digos	10.00	Medium	Iriga	9.20		
13	Medium	Pili	9.20	Medium	Iriga	10.00	Medium	Metro Tuquegarao	9.20		
14	Medium	Metro Tuquegarao	9.00	Medium	Metro Tuquegarao	10.00	Average	Guimba	9.60		
15	Average	Tandag	10.00	Average	Tandag	10.00	Average	Tandag	9.20		
16	Average	Guimba	9.00	Average	Guimba	9.60					
17	Average	Calbayog	8.50								

<b>SEMI CREDITWORTHY</b>											
19			22			23			23		
1	V-Large	Metro Cebu	6.10	V-Large	Metro Cebu	6.20	V-Large	Metro Cebu	7.80	V-Large	Met
2	Large	Metro Kalibo	8.20	Large	San Jose del Monte	8.20	Large	Cagayan de Oro	7.80	Large	Metr
3	Large	Cagayan de Oro	7.80	Large	Cagayan de Oro	7.30	Large	Baquito City	7.70	Large	Bagl
4	Large	Metro Iloilo	7.50	Large	Zamboanga City	7.20	Large	Bacolod City	6.60	Large	San Jose d
5	Large	Cagayan de Oro	7.80	Large	Bacolod City	5.60	Large	Zamboanga City	6.50	Large	Cagayan
6	Large	Metro Iloilo	7.50	Large	Metro Iloilo	5.50	Large	Metro Iloilo	5.90	Large	Zam
7	Large	Zamboanga City	7.50	Big	Metro Roxas	8.20	Big	Camarines Norte	8.40	Large	Met
8	Big	Dagupan	7.30	Big	San Pablo	8.00	Big	Metro Roxas	8.40	Big	
9	Big	Butuan City	8.20	Big	Legazpi City	7.60	Big	Cotabato City	8.40	Big	Legaz
10	Big	Laguna	7.30	Big	Dagupan	7.60	Big	San Pablo City	8.00	Big	Butu
11	Big	Metro Roxas	7.20	Big	Tarlac	7.60	Big	Butuan City	8.10	Big	San Pa
12	Big	Cotabato City	6.80	Big	Camarines Norte	6.50	Big	Dagupan	7.90	Big	Cotab
13	Big	Camarines Norte	6.20	Big	Misamis Occ	5.50	Big	Morong	7.50	Big	Metr
14	Big	Misamis Occidental	5.20	Medium	GMA	8.20	Big	Laguna	7.30	Big	Dagu
15	Medium	Daraga	7.40	Medium	Gen. Santos City	8.10	Medium	Gen. Santos City	7.90	Big	Camarin
16	Medium	GMA	8.40	Medium	Daraga	8.00	Medium	Dumaguete City	7.40	Medium	
17	Medium	Santiago	7.00	Medium	Ilocos Norte	7.80	Medium	Pili	7.50	Medium	
18	Medium	Gen Santos City	6.90	Medium	Pili	7.40	Medium	Santiago	7.50	Medium	
19	Medium	Dumaguete City	6.90	Medium	Santiago	6.60	Medium	Dumaguete City	7.40	Medium	Gen San
20	Medium	Digos	6.00	Medium	Dumaguete City	6.50	Medium	Ilocos Norte	6.70	Medium	
21	Average	Obando	8.00	Average	Marilao	8.00	Medium	GMA	6.10	Medium	S
22	Average	Marilao	8.00	Average	Polomolok	6.00	Average	Marilao	8.00	Medium	Dumagu
23							Average	Polomolok	5.80	Average	

<b>PRECREDITWORTHY</b>											
5			3			3			8		
1	Large	Bacolod City	4.20	Big	Laguna	5.30	Big	Misamis Occidental	5.20	Large	Baco
2	Big	Misamis Occidental	5.20	Average	Obando	5.00	Average	Obando	5.20	Big	Ta
3	Big	Tarlac	4.90	Average	Calbayog City	3.80	Average	Calbayog City	4.60	Big	
4	Medium	Polomolok	5.20							Big	Misamis O
5	Medium	Ilocos Norte	4.70							Medium	Iloc
6										Medium	Calba
7										Average	
8										Average	Pol
41			41			41			41		