

## Speeding Up Road Sector Reform

*Key concerns in the road sector include unsatisfactory preservation of road assets, inadequate investment in the expansion and upgrading of the road network, and slow pace of institutional reforms in the Department of Public Works and Highways (DPWH). There has been considerable progress, despite some delays, in developing technical systems and internal business processes of DPWH, but the associated institutional reforms have lagged far behind. Since both the technical and institutional reforms are necessary to achieve better resource utilization, focusing efforts in the next phase on effecting institutional changes would bring the sector reforms for the national road network much closer to fruition. The empowerment of the Road Board Secretariat, dedication of resources from the Special Road Fund to the maintenance of national roads; and speeding up ongoing efforts to convert DPWH into a commercially-oriented performance-based National Roads Authority are important steps for implementing the institutional reforms. Strengthening the link between user payments and road provision by introducing a fuel levy as an additional source of revenue to the Special Road Fund would help alleviate the under-investment in the road sector.*

### Background

The current road network is 202,000 kilometers of which 15 percent are classified as national roads and 85 percent as local roads. Of these, barangay roads constitute 60 percent of the total network.

The road classification is based on administrative responsibility and not on function and importance. Out of 28,600 km of national roads, only 18,000 km are arterial roads that are best suited to be classified as national roads.

The National Economic Development Authority (NEDA), as head of the Infrastructure Inter-Agency Coordination Committee (INFRACOM), takes the lead in investment planning decisions. The Department of Public Works and Highways (DPWH) is responsible for the national road network while the bulk of the road network (provincial, city, barangay and municipal roads) is managed by respective Local Government Units (LGUs) with DPWH and the Department of Interior and Local Government (DILG) providing technical assistance to them.

Roads are financed primarily through Government budget allocation. The investment program of national roads is funded through the DPWH capital outlay budget while the maintenance program is

appropriated separately using an established formula and is financed, in part, from the recently established Special Road Fund. The investment and maintenance programs for local roads are funded by LGUs through a mix of tax revenues and grants from the Government.

Some progress has been made in implementing the road sector reforms articulated in the 1999-2004 Medium Term Philippines Development Plan (MTPDP) but in general implementation has been slow.

Much of the progress has been in developing technical and information systems for reforming internal business processes of DPWH under the Road Information Management Support System (RIMSS) project. While there have been extensions and delays of up to two years on certain reform components, there have been important achievements.

Agency performance indicators have been developed and some are already in use by DPWH. Road infrastructure surveys have been completed and road and bridge information applications have been developed, including infrastructure performance indicators, which generate reliable data for decision making. Land acquisition procedures have been developed with implementation and staff training on going. New contractor billing systems

reduced average time to pay contractors from 69 days in 2001 to 30 days in 2003. Human resource capacity is being strengthened in parallel to be able handle the new systems.

While the development of a multi-year network planning and programming system is expected in mid July, 2004, the system can be fully operational only after the collection of traffic data, a process which is currently delayed. Another setback has been the delay in the preparation of streamlined contract and procurement documents.

On the institutional side, the Special Road Fund (SRF) was established in 2000 and revenues of P 10.3 billion from the Motor Vehicle User Charge have entered the fund in three years.

However, since the initial establishment of the SRF in 2000, and formal discussions of reform options with DPWH, Department of Budget and Management, Department of Finance and NEDA that led to the development and approval of a plan, there has been little action on the design and establishment of a National Roads Authority.

There has also been little action on the introduction of a fuel levy as an additional source of revenue for the Special Road Fund. Experience in other countries is that road users may be willing to pay for improved roads, provided there is a clear perceived link between the payment and delivery of better services. Furthermore, the administration of the Special Road Fund has been subjected to external pressures, in delaying and diverting the release of funds, so that it has not been as effective as expected in improving the road maintenance program.

The lack of significant progress on the institutional reforms is a high risk that would impede the overall success of the DPWH reform program and greatly reduce the potential benefits of the technical system reforms.

## **Main Issues**

The two key issues hindering the efficient performance of the road system are: (i) the unsatisfactory preservation of the road assets; and (ii) the inadequate investment in the expansion and upgrading of the road network.

There are two main contributors to these problems. The first is the weak institutional framework and capacity of the sector including poor governance and corruption. This leads directly to inefficient resource utilization. The second reason is the relatively low level of contributions to the road system by the government and the private sector.

### ***Unsatisfactory Preservation of Road Assets***

Manifestations of the unsatisfactory preservation of the road assets for both national and local roads are discussed below.

#### ***National Roads***

The annual requirement for the maintenance of the national road network is estimated at about 16 billion 2003 Pesos<sup>1</sup> but actual expenditures for the past year were about 4.0 billion Pesos, or only 25 percent of estimated requirements. Despite the government's attaching the highest priority to the maintenance of existing road assets in the 1999-2004 MTPDP, maintenance spending for the past five years has varied between 25 and 30 percent of requirements, indicating that the condition of national roads has been consistently deteriorating throughout this period.

While the lack of reliable historical data precludes establishing how much the road assets have deteriorated in the past, recent investigations of road conditions covering 10,000 km of paved roads indicated that half of these roads were in poor condition.<sup>2</sup> The road condition data was for the north south

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<sup>1</sup> World Bank estimates based on data from the Better Philippines Roads Study in 1999.

<sup>2</sup> Based on the International Roughness Index (IRI)—an IRI of 5 or higher resulted in a classification of poor.

backbone and the east-west laterals among other strategic roads that receive priority in maintenance.

Moreover, present maintenance practices are likely to be inefficient since most of the maintenance is carried out by administration and, even when carried out by contract, the administration limits scope for private sector efficiency by defining specific activities for the private contractors to carry out.

Maintenance funds are periodically used to finance labor-intensive employment-generation programs. Most recently, about 2 billion (or 50 percent) of the amount released from the Special Road Fund has been used to fund employment generation programs which are more than five times as expensive as competitive procurement of the required services by contract.

#### *Local Roads*

With a few exceptions, there are no expenditure recording and information systems in LGUs to provide reliable estimates on maintenance spending or road conditions. A study by the Asian Development Bank indicates that spending on the preservation of the 172,000 km local road network is one quarter of estimated requirements.<sup>3</sup> The expenditure on maintenance of local roads was about P 3.1 billion in 2002 or P 18,000 per km, significantly lower than the required P 13.9 billion or P 80,000 per km.

#### ***Inadequate Investment in Expansion and Upgrading of the Road Network***

Investment in the road network is low. Total expenditures (both investment and maintenance) on roads as a percentage of GDP declined steadily from a high of 1.4 - 1.50 percent of GDP in 1999 to a decade-low level of about 0.75 - 0.80 percent in 2002. This is significantly lower than what is required. Actual expenditures on roads as a percentage of GDP show large variations for the different countries in the region with

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<sup>3</sup> Cradno MBK Pty Ltd, "Rural Roads Development Policy Framework", Asian Development Bank (Nov 2003).

Vietnam and China spending 2.7 and 3.5 percent of their respective GDPs on roads; and Thailand and Indonesia spending about 1.1 and 0.5 percent respectively.

To maintain its existing network and invest in roads to support and sustain annual economic growth of 5 percent, for example, the required expenditures on the road network would be in the order of 2 percent.<sup>4</sup> The current government inclination to freeze the national road investment budget at its 2003 level through 2009 would result in significantly lower levels of investment as a percentage of GDP. This may be withstood by a country for a year or two but cannot be sustained for a long period of time without adversely affecting growth.

Only about 80 percent of arterial national roads are paved. The pavement of all arterial roads is generally well justified on economic and social grounds as they both carry sufficient traffic volumes and are essential for linking provinces to the country's various economic growth centers and facilities.

The implementation of several foreign-assisted projects has been delayed due to the lack of counterpart financing.

The under investment in capacity manifests itself in increasing levels of congestion. A study prepared by the National Center for Transportation Studies for NEDA and the Legislative-Executive Development Advisory Council in 2000 indicated that losses due to congestion in Metro Manila were around 100 billion Pesos per year in 1996 prices.

There is also an increasing need for roads bypassing towns, to overcome significant reductions in travel speeds and to reduce the rates of traffic accidents and casualties in

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<sup>4</sup> The estimate is based on a formula developed by the World Bank to give orders of magnitude. According to this formula, investment needs for the road sector would be 0.25 percent of projected GDP growth (for a growth of 5 percent, the required investment in roads would be 1.25 percent of GDP). The balance of 0.75 percent reflects the maintenance requirements.

these towns. In some cases, the benefits of a road network are not fully realized due to missing links and lack of inter-connectivity of some expressways.

### **Main Reasons for the above problems**

#### **Inadequate policy and institutional frameworks and capacity....and slow progress of reforms**

##### *National Level*

*Weak commercial orientation of DPWH.* Progress by DPWH has been slow in implementing the institutional reforms. While the development of the technical systems necessary to re-engineer its internal business processes are progressing after some delay, there has been no progress on converting DPWH into a commercially-oriented National Roads Authority. The high-level multi-agency oversight group that was to be established by NEDA to monitor and drive the reform process has still not convened or taken control of the reform process 18 months after this was decided.

*Perceptions of corruption.* Recently released results of the June 2004 Social Weather Stations Enterprise Survey revealed that the public's perception of DPWH's efforts to combat corruption is one of the worst among public agencies, and has further worsened over the past two years. The lack of a strong governance framework in DPWH is likely to result in uncompetitive procurement practices and reduced quality of road construction, which reduce efficiency and add significantly to the cost of road provision.

*Lack of clear direction by the Road Board.* Although the administrative order was set up in early 2003, the head of the Road Board has only been recently appointed, and a Road Board Secretariat is now only being established after long delays in authorizing the staffing and budget status. Without the focused guidance of the Secretariat, the Road Board runs the risk of developing objectives and processes that are heavily influenced by the political process and conflict with many reform objectives.

*Overstaffing in DPWH.* Out of 35,000 employees, about 60 percent are allocated to roads. This translates into 1.4 km of national roads per employee compared to 9 km per employee in Indonesia, for example.

##### *Local Level*

Most LGUs do not have prioritized Investment Programs and spending is not according to a plan. In many cases there appears to be very little systematic planning as to how funds are allocated and no formal analysis of investments or prioritization based on efficiency criteria.

The devolution of responsibilities to the LGUs was not accompanied by building their planning, technical and implementation knowledge and skill base. Planning and programming, in particular, have been pointed out as the weakest points in the project management cycle. It would be beneficial to devote special attention to the management of local roads given that a large percentage of the expenditures of LGUs on infrastructure (excluding housing), is on roads.

Resources for investment in local roads come from different sources with little coordination among them. These include the Department of Agriculture, the Department of Agrarian Reform, LGUs and the Congressional Initiatives. The first two departments finance farm to market roads. These road investments are typically conceived in the context of an agricultural or irrigation project and not as part of an overall road development plan. Moreover, little attention is typically paid to the maintenance requirements and sustainability of these roads.

As more than one level of local government can be directly involved in the management of certain sections of the road network, there is bound to be functional overlap as well as fragmentation in responsibilities.

DPWH receives budgetary allocation from the congressional initiative fund (CIF) for expenditure on local roads. This amount has varied between 19 and 30 percent of DPWH's budget. The efficiency of use of

CIF funds could be significantly improved if linked more closely to municipal development priority plans and normal standards of design and economic analysis.

Appropriations from the CIF (roads, flood control, etc.) are all included under one title “various infrastructure” in DPWH’s budget. Consequently, expenditures out of this line item are not transparent.

With few exceptions, no detailed assessment of the organization, system and procedures and staff competence has taken place in Road Management Units in LGUs.

### ***Low levels of contribution by government and private sector***

#### *National Government*

The increasing government deficit has resulted in a reduction in the budgetary resources committed to the road sector over the past five years both in real terms and as a percentage of GDP. Budgetary resources to the sector are likely to increase once the fiscal deficit is reduced and efficiency of the sector in resource utilization is enhanced.

#### *Private Sector*

Private sector participation in the Philippines started in the road sector in the 1970’s but interest has waned since then despite the enactment of the BOT law in 1990’s. In the last decade, only four agreements were concluded, one of which never got started, two are stalled after completion of a phase and the fourth is expected to be completed this year after lengthy delays.

The interest and contribution of the private sector to investment in the road network has been low for a number of reasons. Inability of the private sector to come up with the necessary financing is due in large part due to the uncertainty surrounding the investment climate and the legal environment in addition to problems in acquiring right of way.

Of 16 road projects being monitored by MMDA, 11 are encountering right of way problems. A law enacted in 2000 to

facilitate the acquisition of right-of-way for infrastructure projects has had little impact so far. The delays are due to (i) the identification of the beneficiaries and the valuation which often end up in lengthy court proceedings; (ii) reluctance of government to use its power of eminent domain and reliance on negotiation; and (iii) complexity arising from the need to deal with more than one LGU.

### **Recommendations**

A strong partnership between the private and public sectors would help enhance the effective and efficient development and management of the sector. The public sector, will play the lead role, developing good plans (through collaboration with the private sector), ensuring efficient utilization of its limited resources and providing an enabling environment for the participation of the private sector. These objectives can be met by re-aligning policies according to principles of sound economic management, strengthening institutions, building capacity, developing a strong governance framework and culture and weeding out corruption.

Many of the necessary reform measures have been identified by the Government in the past and set as targets in the MTPDP. As of today, only a few of the targets have been met, and many of the reforms have either stalled or have been delayed.

#### *For Efficient National Road Management*

There has been considerable progress, despite some delays, in developing technical systems as part of the reforms of the internal business processes of DPWH but the associated institutional reforms have lagged far behind. A focus in the next phase on effecting institutional changes would bring the sector reforms much closer to fruition and would result in a more efficient utilization of scarce resources. More specifically this would involve:

- Convening the high-level multi-agency oversight group to monitor and drive the road sector reform process.

- Setting up and empowering the Road Board Secretariat and strengthening the Road Board's control over use of funds through well defined ownership and oversight of the Special Road Fund.
- Establishing a commercially-oriented performance-based National Roads Authority.
- Further strengthening the link between user payments and provision of roads by augmenting the receipts of the Special Road Fund by revenues from the fuel levy. This would also help ease the current under-investment in the road sector
- Speeding up the ongoing reclassification of secondary national roads into lower level local roads to enable DPWH to better focus on the management of the core arterial roads.
- Increase transparency in decision making to change the widely prevalent perceptions of corruption in DPWH.

#### *To Encourage Private Sector Participation*

- The commitment of the government to resolving outstanding issues in toll road agreements is likely to have a positive impact on attracting private sector participation in the construction and operation of toll roads. Focusing on one or two toll roads (STAR & R-1 Expressways, for example) may provide the necessary signal.
- As right of way acquisition remains a deterrent to private sector participation in the sector, it would be beneficial to analyze and resolve obstacles in implementation of the new right-of-way law. Extracting good practices from past right-of-way acquisition and disseminating them for wider application could be helpful.
- Use open competition as the preferred method for project selection. Unsolicited proposals, if considered, should be subject to especially rigorous analysis and monitoring.

#### *For Efficient Local Road Management*

Recommendations in this area will enforce some of the broader key reform opportunities and capacity building plans for LGUs addressed in other briefs devoted to local government issues. The focus below will be on road-specific issues.

- The efficiency of congressional initiative investment in local roads can be greatly enhanced, if the approval of projects is subject to rigorous efficiency criteria and if they are part of local government investment plans.
- As several national agencies and institutions (Department of Agriculture, Department of Agrarian Reform) have mandates for investing in local roads, coordination mechanisms for harmonizing the efforts of the different government agencies and different levels of local government would enhance the effectiveness of the local road network in efficiently addressing the access and poverty alleviation as well as growth objectives of the road sector.
- For the effective preservation of the local road network, it would be necessary to strengthen LGU capacity to manage existing road assets and develop a simple information database of existing roads and their conditions as a step towards efficient management.