



Republic of the Philippines
DEPARTMENT OF FINANCE
Roxas Boulevard Corner Pablo Ocampo, Sr. Street
Manila 1004

DEPARTMENT ORDER NO. 031.2018
04 May 2018

SUBJECT: GUIDELINES ON THE COMPUTATION AND CERTIFICATION OF INCOME FOR THE CREATION, CONVERSION, MERGER OR ABOLITION OF A LOCAL GOVERNMENT UNIT (LGU)

1.0 RATIONALE

This Department Order establishes the rules and guidelines in the attestation or certification of income relative to the requirement of law in the creation, conversion, merger, or abolition of local government units (LGUs). Pursuant to Sections 7, 8 and 9 of Republic Act (RA) No. 7160, otherwise known as the Local Government Code (LGC) of 1991, and RA No. 9009¹, the Department of Finance (DOF) is mandated to attest the income indicator in the creation, conversion, merger or abolition of LGUs. Likewise, the provincial treasurer and the city treasurer are mandated by the LGC to certify the income requirement for the creation of municipalities and for the classification of a city into a highly urbanized city, respectively.

2.0 LEGAL BASES

- 2.1 Section 7 of the LGC requires that the creation of an LGU or its conversion from one level to another level shall be based on verifiable indicators of viability and projected capacity to provide services, to wit: (i) income; (ii) population; and (iii) land area. The income of such LGU *must be sufficient, based on acceptable standards, to provide for all essential government facilities and services and special functions commensurate with the size of its population, as expected of the local government unit concerned;*
- 2.2 Section 8 of the LGC prescribes that the division and merger of existing LGUs shall comply with the same requirements of Section 7 of the LGC. However, such division *shall not reduce the income, population, or land area of the local government unit or units concerned to less than the minimum requirements prescribed in this Code: Provided, further, That the income classification of the original local government unit or units shall not fall below its current income classification prior to such division.*
- 2.3 Section 9 of the LGC further mandates that an LGU *may be abolished when its income, population, or land area has been irreversibly reduced to less than the minimum standards prescribed for its creation under Book III of the LGC, as certified by the national agencies mentioned in Section 17 of the LGC to Congress or to the sanggunian concerned, as the case may be.*

¹ An Act Amending Section 450 of Republic Act No. 7160, otherwise known as the Local Government Code of 1991, by Increasing the Average Annual Income Requirement for a Municipality or Cluster of Barangays to be Converted into a Component City

- 2.4 The income requirement for the conversion of municipality or a cluster of barangays into a component city and for the creation of a province shall be certified by the DOF, pursuant to Section 450(a), as amended by RA No. 9009, and Section 461(a) of the LGC, respectively.

For the conversion into a component city, the required locally generated average annual income for the last two (2) consecutive years shall be at least One Hundred Million Pesos (Php100,000,000.00) based on 2000 constant prices. While the required average annual income for the creation of a province shall be not less than Twenty Million Pesos (Php20,000,000.00) based on 1991 constant prices. *Provided*, That the creation thereof shall not reduce the income of the original unit or units at the time of said creation to less than the minimum prescribed requirements.

- 2.5 The income requirement for the creation or conversion to a municipality and classification into highly urbanized city shall be respectively certified by the provincial and city treasurer, pursuant to Section 442(a) and Section 452(a) of the LGC.

For the creation of a municipality or conversion of a barangay into a municipality, the required average annual income for the last two (2) consecutive years shall be at least Two Million Five Hundred Thousand Pesos (Php2,500,000.00), based on 1991 constant prices. *Provided*, That the creation thereof shall not reduce the income of the original municipality or municipalities at the time of said creation to less than the minimum requirements prescribed herein. While the required latest annual income for the classification into a highly urbanized city shall be at least Fifty Million Pesos (Php50,000,000.00) based on 1991 constant prices.

- 2.6 Sections 442(c), 450(c), as amended, and Section 461(c) of the LGC, defines the composition of the average annual income as the income accruing to the general fund, exclusive of special funds, trust funds, transfers and non-recurring income.

- 2.7 Under Department Special Order No. 6-92 dated August 21, 1992, or the Code of Approving and Signing Authorities, the Bureau of Local Government Finance (BLGF) of the DOF is mandated to certify the income of LGUs.

- 2.8 Under Department Order 08-2011 dated 11 February 2011, the electronic Statement of Receipts and Expenditures (eSRE) is the official reporting system of the DOF on local fiscal and financial matters, to be maintained by the DOF-BLGF to fully establish a reliable, accurate and timely reporting and monitoring system in the country.

- 2.9 Resolution No. 2, series of 2009, entitled "Approving the Synchronized Rebasing of Price Indices to Base Year 2006" of the National Statistical Coordination Board (NSCB), now known as the Philippine Statistics Authority (PSA), has approved the rebasing of the price indices to base year 2006. The PSA has declared through its letters dated 04 November 2014 and 10 May 2016 that the old Consumer Price Index (CPI) series will no longer be generated once the new or rebased series becomes available.



3.0 PURPOSE

This Department Order shall be used by the BLGF and the provincial and city treasurers in attesting and certifying the income requirement for purposes required by the LGC to ensure uniformity in the computation thereof.

4.0 BASIC DATA

The BLGF and the concerned provincial and city treasurers shall use the approved Statement of Receipts and Expenditures (SRE) submitted by the LGUs through eSRE system for the last two (2) consecutive years, and four (4) years prior to the issuance of the latest income reclassification, as the basic data for computing and attesting the income requirement.

5.0 FEATURES OF THE CERTIFICATION

The certification of the average annual income shall be comprised of the following income requirements:

- 5.1 Average Annual Income of Proposed LGU;
- 5.2 Resulting Average Annual Income of the Original LGU or LGUs (in determining whether the income of the original unit or units at the time of the creation or conversion will be reduced to less than the minimum requirements prescribed in the LGC); and
- 5.3 Resulting Average Annual Regular Income of the Original LGU or LGUs (as basis of the income classification of the original LGU or LGUs at the time of said creation or conversion).

6.0 DETERMINATION OF ANNUAL INCOME

Based on the definition of annual income cited in the LGC and RA No. 9009, it shall be composed of income accruing to the general fund, exclusive of special funds, trust funds, transfers and non-recurring income, and computed as follows:

- 6.1 Creation of Province, Creation of Municipality or Conversion of Barangay into Municipality, and Classification of Component City into Highly Urbanized City:

$$\begin{array}{l} \text{Annual} \\ \text{Income} = \end{array} \begin{array}{l} \text{Real Property Tax (General Fund) + Tax on Business + Other Taxes + Regulatory} \\ \text{Fees (Permits and Licenses) + Service/User Charges (Service Income) + Receipts} \\ \text{from Economic Enterprises (Business Income) + Interest Income + Shares from} \\ \text{Philippine Economic Zone Authority (PEZA) + Internal Revenue Allotment (IRA)} \end{array}$$

- 6.2 Conversion of Municipality/ies or Cluster of Barangays into Component City:

$$\begin{array}{l} \text{Locally} \\ \text{Generated} \\ \text{Annual} \\ \text{Income} = \end{array} \begin{array}{l} \text{Real Property Tax (General Fund) + Tax on Business + Other Taxes + Regulatory} \\ \text{Fees (Permits and Licenses) + Service/User Charges (Service Income) + Receipts} \\ \text{from Economic Enterprises (Business Income) + Interest Income + Shares from} \\ \text{PEZA} \end{array}$$



7.0 COMPUTATION OF THE AVERAGE ANNUAL INCOME BY INDEXING

7.1 In the absence of the PSA-issued CPI based on the required base year, the BLGF shall compute the CPI factor and apply to the average annual income at current prices using the following steps of indexing approach:

- 7.1.1 Compute the growth rate of CPI based on available constant price released by PSA for fiscal year (t) by dividing the difference of current year and prior year CPI based on available constant prices to prior year CPI based on available constant price.

$$\text{Growth Rate of CPI based on available constant prices}_t = \frac{\text{CPI based on available constant price}_t - \text{CPI based on available constant price}_{t-1}}{\text{CPI based on available constant price}_{t-1}}$$

- 7.1.2 Estimate the CPI based on required constant price of fiscal year (t) for the creation of province/municipality and conversion into component city using the computed growth rate of CPI based on available constant price.

$$\text{Required CPI}_t = \frac{(1 + \text{Growth Rate of CPI based on available constant price}_t) \times \text{Required CPI}_{t-1}}$$

The CPI based on required constant prices is 100. Hence, computation of the required CPI factor shall be as follows:

$$\text{Required CPI factor}_t = \frac{\text{CPI based on Required Constant Price}_t}{100}$$

- 7.1.3 Divide annual income at current prices by the CPI factor based on required constant prices, depending on the LGU type to get the annual income at constant price.

$$\text{Annual income at constant prices (AICP)}_t = \frac{\text{Annual income at current prices}_t}{\text{Required CPI factor}_t}$$

7.1.3.1 Creation of Province: compute the annual income at constant prices received by the province from all the subject municipalities.

7.1.3.2 Conversion into Component City: compute the locally generated annual income at constant prices of component municipality or cluster of barangays.

7.1.3.3 Creation of Municipality: compute the annual income at constant prices received by all the subject barangays.

7.1.3.4 Classification of Component City as Highly Urbanized City: compute the latest annual income at constant prices of the subject component city.

- 7.1.4 Add each annual income at constant price for a given year to get the total annual income and divide the total annual income by the number of fiscal years to get the average annual income based on constant prices.

$$\text{Average Annual income at constant prices (AICP)}_{t1, t2} = \frac{\text{AICP}_{t1} + \text{AICP}_{t2}}{2}$$



- 7.2 To determine if the creation or conversion of an LGU will not reduce the income of the original unit or units at the time of said creation or conversion to less than the minimum requirements prescribed in the LGC, compute the reduced average annual income of the original unit or units by deducting the shares of income of the proposed LGU to the annual income of the original unit or units.

8.0 RESULTING INCOME CLASSIFICATION OF THE ORIGINAL LGU/LGUs

The average Annual Regular Income of the original LGU/LGUs less than its shares from the proposed LGU at current prices, shall be the basis in determining the resulting income classification of the original LGU/LGUs, based on existing policy of the DOF on income classification.

9.0 RESPONSIBILITIES OF THE BLGF

The BLGF, being the policy and technical arm of DOF in supervising the revenue operations of all local governments, shall implement this Order and shall be responsible for the following:

- 9.1 Update annually the CPI Factor based on the available CPI data released by the PSA;
- 9.2 Provide annually the matrix of CPI table to be used by the provincial and city treasurers in computing and certifying the latest annual income;
- 9.3 Issue the Certificate of Average Annual Income to requesting LGUs and legislators, as prescribed in the LGC, indicating the results of the abovementioned income requirements;
- 9.4 Capacitate provincial and city treasurers on the process and methodology of computing and certifying the latest annual income;
- 9.5 Issue appropriate clarificatory guidelines/updates/advisories relative to the implementation of this Department Order subject to the direct supervision and approval of the Undersecretary of Revenue Operations Group; and
- 9.6 Provide an annual report to the DOF on the certifications issued.

10.0 REPEALING CLAUSE

All department orders, circulars and issuances inconsistent with this Department Order are hereby repealed or modified accordingly.

11.0 EFFECTIVITY

This Department Order shall be effective fifteen (15) days after completion of its publication in a newspaper of general circulation.




CARLOS G. DOMINGUEZ

Secretary
JUN 08 2018