MUNICIPAL REFORM AND DEVELOPMENT PROGRAM

(AR-0250)

EXECUTIVE SUMMARY

BORROWER AND GUARANTOR:	The Argentine Nation	
EXECUTING AGENCY:	Ministry of the Interior	
AMOUNT AND SOURCE:	IDB (ordinary capital):	US$250 million
	Local counterpart funding:	US$250 million
	Total:	US$500 million
FINANCIAL TERMS AND CONDITIONS:	Amortization period:	20 years
	Grace period:	5 years
	Disbursement period:	5 years
	Interest rate:	variable
	Inspection and supervision:	1%
	Credit fee:	0.75%
	Currency:	U.S. dollars, Single Currency Facility

OBJECTIVES:

The primary objective of the program is to set in place institutional conditions for self-sustaining development of Argentina's municipalities. Its specific objectives are: (i) to promote sustainable fiscal-account balancing by boosting municipal revenues, reducing and tightening controls on expenditure, and bringing in integrated financial management systems; (ii) to make for more efficient and better-managed city utility and local social service delivery; (iii) to modernize the municipalities' internal administration systems and train municipal employees; and (iv) to help devise financing mechanisms whereby municipalities can tap the capital markets, to secure medium- and long-term funding for their capital investment projects.

DESCRIPTION:

The starting point of the program will be negotiations with the participating municipalities for the adoption of fiscal adjustment targets, institutional reforms, and investment financing. The program will be open to any Argentine municipality which is prepared to carry through the type of institutional and management-modernization reforms that will come in for support under the program. These reforms will be described in Reform and Investment Plans to be agreed upon as a condition for municipalities to join the program; attainment of the

plan targets will be reviewed annually. Once targets have been agreed upon, the program will finance the following components:

1. Municipal reforms component (US$200 million). This component will support reforms in municipal administrative and management tools, specifically in the areas of (i) financial management and tax administration, and (ii) internal management and efficiency of government services.

2. Investment component (US$277 million). Funding will be provided for investment projects in the following sectors: (i) urban roads; (ii) storm drains and erosion and flood control structures; (iii) social services such as health posts, preschool facilities, and seniors' homes; and (iv) city services such as trash collection and disposal, street lighting, parks and other green spaces, and recreation.

3. Municipal private borrowing component (US$2 million). The program will help set up a mechanism whereby municipalities already reformed can more readily gain access to long-term funding from the private sector. A study will look at financial intermediation arrangements that could be devised for municipalities to secure long-term market finance for municipal projects, on a sustainable basis.

THE PROGRAM'S ROLE IN THE BANK'S COUNTRY AND SECTOR STRATEGY: The Bank's strategy for its operations with Argentina calls for support for three core areas of action: (i) poverty reduction and improving the quality of life of Argentina's people, by creating employment and expanding coverage of basic services; (ii) raising productivity and heightening competition in domestic production; and (iii) deepening and consolidating reforms of the State and extending such modernization efforts to the provinces and municipalities.

The program proposed here fits within the aforementioned strategy, inasmuch as it will support tax, financial, and institutional reforms intended to assure fiscal and financial sustainability of the country's municipalities, along with adequate coverage and quality of municipal services.

ENVIRONMENTAL AND SOCIAL REVIEW: The executing agency has produced an environmental impact assessment and devised Program Environmental Control Procedures. The proposed activities would leave individual municipalities with a healthier

environmental balance sheet. Any mild adverse effects the investment projects might have on the environment, during construction or thereafter, could be readily mitigated. The environmental assessment and management procedures included in the Operating Regulations will assure environmental quality (see paragraphs 4.13 to 4.16 of the proposal which follows).

BENEFITS: The main benefit of the program will be an increase in municipally generated revenues and more efficient use of those funds, deriving from the reform projects carried through in each municipality. The program also will help instill greater discipline for investment funding allocation, once project appraisal practices are adopted to prioritize investment projects by reference to their overall viability (technical, financial, economic, environmental). The program's direct economic benefits will be those ensuing from the investment projects it funds.

RISKS: The risks associated with this program have to do with possible delays in implementing institutional reforms because of the new laws that will be required in some instances, and the requisite internal administrative changes. The best way to minimize these risks is to build into the program incentives for municipal governments to adopt major changes — one such incentive being the prospect of refinancing their debt — as a condition precedent to receiving funding for priority investments. Moreover, the proposed Central Executing Unit, working proactively and in concert with the provinces, will get the necessary processes going and expedite them, and help build consensuses with local communities.

Adjustments to taxation instruments in line with the Federal Fiscal Pact may diminish municipalities' own revenues. Countering this eventuality will be the planned tax-administration strengthening projects, which will boost tax yields, and the adoption of revenue-sharing arrangements to offset eventual revenue losses, as also provided in the Federal Fiscal Pact.

SPECIAL CONTRACTUAL CONDITIONS: **Conditions precedent to the first disbursement:** (i) the Central Executing Unit must have been placed in charge of the program's implementation and must have the personnel and funds it needs to perform that function properly (paragraph 3.5); (ii) the program's Operating Regulations must be in effect (paragraph 3.29); (iii) the final Reform and

Investment Plan model must have been submitted to the Bank's satisfaction (paragraph 3.29); (iv) the borrower must have executed 15 subsidiary loan agreements with municipalities eligible for the program (paragraph 3.29); and (v) a special account must have been opened with the Fiscal Agent to take receipt of disbursements of the program funds (paragraph 3.29).

Other special conditions: (i) six months after the effective date of the loan contract, the executing agency is to demonstrate that it has hired, to the Bank's satisfaction, sufficient consulting firms to supervise the reform projects pertaining to operations planned for year 1 of the program (paragraph 3.7); (ii) within 90 days after the effective date of the loan contract the executing agency must demonstrate that it has distributed a copy of the program's Operating Regulations, along with other pertinent information, to all Argentine municipalities (paragraph 3.30); and (iii) as a condition for disbursing the municipal private borrowing component, the executing agency must present, to the Bank's satisfaction, terms of reference for the studies to be commissioned (paragraph 3.30).

POVERTY-TARGETING AND SOCIAL-SECTOR CLASSIFICATION: Since this project will benefit the Argentine people at large, with no slant toward any specific group, it would not qualify as poverty-targeted under the terms of paragraphs 2.13 and 2.15 of the Eighth Replenishment document (AB-1704), or as a poverty-reduction operation.

EXCEPTIONS TO BANK POLICY: None

PROCUREMENT: In keeping with Bank policies, when proceeds of the loan are to be used and the purchaser is the public sector, international competitive bidding will be mandatory for construction contracts of US$5 million and up and for goods costing US$350,000 or more. The Bank's Country Office in Argentina will do ex post sampling reviews of construction contracts of under US$3 million and contracts for goods valued at less than US$350,000, with ex ante reviews of each step in the procurement/contracting process in which the Central Executing Unit is involved for the first time.

Likewise in accordance with the Bank's policies, international competitive bidding will be required to

engage consultants on contracts of over US$200,000. The Country Office will do ex post sampling checks of consulting-firm contracts worth less than US$200,000 equivalent and individual-consultant contracts below US$50,000. However, when the Central Executing Unit is acting for the first time at any stage in the procurement and contracting process for this program, the Bank will do an ex ante review for each stage.

I. FRAME OF REFERENCE

A. The municipal public sector

1. Introduction

1.1 Argentina is a federal union with 23 provinces, an autonomous metropolis (Buenos Aires), 1,123 municipalities, and 800 *comunas*. 1/ The federal government's authority is expressly delegated to it by the provinces, which in turn have autonomy to configure their municipal systems. Municipalities thus make up the subprovincial structure of government, with jurisdiction in their respective territory. Every municipal government has a deliberative body and an executive; both mayors and council members are elected every four years.

1.2 The vast majority (87%) of Argentina's population of 32.6 million live in large towns and cities. The population breakdown for the 1,123 municipalities is given in Table I-1.

1.3 This population distribution pattern bespeaks very diverse economic and social conditions and widely varying technical and government management capabilities. The country is now resolutely engaged in a gradual decentralization process, which is posing serious challenges to the authorities in terms of bringing in technical assistance and financing mechanisms that can assure sound social- and city-service delivery to the entire population.

Table I-1: Population breakdown

Population size range	No. of municipalities	% of population
Under 10,000	753	13.7
10,000 – 250,000	345	43.0
Over 250,000	24	34.3
Buenos Aires	1	9.0
Total	1,123	100.0

2. Fiscal decentralization

1.4 Between 1994 and 1997 Argentina's provinces and municipalities together accounted for 50% of the country's aggregate public spending (40% and 10% of the total, respectively). Considering that subnational governments' share of total expenditure averages less than 15% in Latin America overall, Argentina clearly is highly decentralized for a country in this region. The figures are particularly telling where social expenditure is concerned: the provinces and municipalities together are responsible for 80% of the country's social spending (63% and 17%, respectively, of the total).

1/ Loosely defined, a *comuna* is a jurisdictional district with a population of up to 10,000, which comes directly under the respective provincial government.

Table I-2
Provincial-municipal transfers: the case of the Province of Mendoza

The pool of federal and provincial tax revenues that is shared out to the municipalities is as follows:

(1) Primary distribution: 14% of federal receipts from the VAT, profits tax, fuel tax, and other federal taxes go to the municipalities, together with 14% of provincial revenues from the gross-receipts tax, property tax, and stamp tax. Municipalities also receive 70% of provincial vehicle license tax revenues and 12% of provincial oil, uranium, electric power, and gas royalties. A number of provinces, Mendoza among them, have set up equalizing funds to compensate for differences in development status of their municipalities.

(2) Secondary distribution: In the province of Mendoza, the formula for apportioning the revenue-sharing pool described in point (1) is as follows: (i) 25% divided equally among all the municipalities; (ii) 65% distributed pro rata to the municipalities' populations; and (iii) 10% by reference to a regional development equalization ratio.

1.5 Decentralization is much less in evidence where taxing authority is concerned: the provinces and municipalities currently bring in the equivalent of 25% of the country's aggregate tax revenues (20% and 5%, respectively, of total intake). The discrepancy in their powers on the revenue and expenditure sides has given birth to a convoluted structure of shared revenues and functions based on a system of intergovernmental transfers and tax share-outs which vary from province to province see Table I-2). Operating in tandem with the federal-provincial tax-sharing scheme 2/ are a series of interprovincial and provincial-municipal sharing arrangements. The fiscal-power disparity between spending responsibility and taxing authority is particularly pronounced at the municipal level: in virtually every case, municipalities may collect only rates and betterment levies, and receive a portion of national and provincial tax intakes (see Table I-3). Moreover, the modest yields of many municipally based levies are by no means proportional to what it costs the municipalities to administer them.

1.6 This revenue-sharing scheme affects particularly those expenditure items for which the three levels of government share responsibility, as is the case with education. It also has a critical impact on municipal revenues, since one part of the revenue-sharing pool is a percentage of the proceeds of levies like the property tax which, according to municipal spending responsibilities, should fall fully under municipal jurisdiction.

2/ Proceeds of the following federal taxes go into the revenue-sharing pool for the provinces: VAT (80% of total proceeds); profits tax (64%), the fuel tax, and some other minor levies. Net revenue share-outs to the provinces as a whole for 1998 are expected to be 57% of aggregate revenues from these federally collected taxes. Since 1994, the national government has guaranteed a minimum of 740 million pesos monthly in share-outs to each province; funds are automatically transferred each day.

1.7 An important consideration here is the constraints that this apparatus means for subnational governments seeking to fund their own operations. From 1994 to 1997, for instance, municipalities funded an average 52% of their aggregate expenditure with own resources, and the balance through resource transfers (largely revenue share-outs) from other levels of government; the provinces funded only 45%. Table I-3 shows how responsibility for public spending and taxing authority is spread among the three levels of government.

Table I-3
Government responsibilities, by level of government

A. Spending responsibility and chief functions			
National government	**National government and provinces**	**Provinces and municipalities**	**Municipalities**
Defense Foreign affairs Highways Trade regulation	Economic development Higher education Justice and social security Regional infrastructure Housing	Basic education Polymodal education Health Sanitation Roads Civil defense	City streets City sanitation Street lighting Drainage Parks/green spaces City planning

B. Taxing authority		
National government	**Provinces**	**Municipalities**
Value-added tax Social security taxes Income taxes Fuel taxes Foreign trade levies Consumption taxes Personal property tax	Gross receipts Property tax 1/ Stamp tax Vehicle license tax Payroll tax	Utility rates Street lighting and sanitation levy Cemetery tax Betterment levies

1/ In some provinces the property tax and vehicle license tax are collected by the municipalities.

3. Municipal fiscal accounts in recent years

1.8 Between 1994 and 1997 municipal government deficits widened, the result of 3% growth in spending that outstripped 2.5% rises in revenue. In 1995, against a backdrop of severe recession in Argentina, the municipalities posted a surplus, in the wake of sharp cuts in spending and declines in own revenues, offset in part by increased extraordinary central government transfers and debt service. In the two following years, the rapid rise in municipal spending and slow recovery of own revenues wiped out what had been a temporary surplus (US$60 million), leaving the municipalities with a deficit twice as high (US$125 million).

Table I-4
Municipal government revenues and expenditures
(millions of pesos)

	1994	1995	1996	1997	Annual change (average)
Total revenues:	6,493	6,367	6,519	7,002	2.5%
Municipally generated	3,261	3,026	3,245	3,227	(0.3%)
Transfers	3,232	3,341	3,274	3,775	5.3%
Total expenditure:	6,519	6,307	6,579	7,127	3.0%
Municipal administration	2,302	2,247	2,354	2,533	3.2%
Social services	3,534	3,410	3,541	3,854	2.9%
Economic services	656	607	638	691	1.7%
Public debt (interest)	27	43	46	49	21.9%
Surplus (deficit)	(26)	60	(60)	(125)	68.8%
Memorandum items:1/					
Current saving/own resources	10.5%	5.1%	7.7%	9.0%	-
Funded debt/own resources	n.a.	25.9%	23.2%	23.5%	-
Debt service/own resources (interest and principal)	n.a.	8.7%	8.9%	12.1%	-

1/ Selected ratios for a representative sample of 480 municipalities.

1.9 Of the foregoing expenditure items, the rise in municipal administration costs did the most to push up total municipal outlays. This was the result of a 6% increase in the wage bill combined with a 2% increase in municipal government employment. The higher wage bill, in turn, stemmed from increases in social security charges (pension contributions) and union-administered social-fund contributions, which then were subtracted directly from revenue share-outs received by the municipalities.

1.10 To contend with these rising expenditures and low taxing capacity, the municipalities adopted a series of measures to keep their deficits in check, among them: (i) short-term borrowings from commercial banks at steep market rates, often as high as 24% per annum; (ii) delaying payments to suppliers; (iii) creating new taxes; and (iv) hiking rates and prices for government services and utilities. Except where these measures were purely temporary solutions, they have created financial difficulties for the municipalities, leaving them with fiscal shortfalls that will not easily be made up – particularly considering the low current saving figures shown in Table I-4.

4. <u>Municipal debt</u>

1.11 At year-end 1997 the estimated debt stock of a representative sample of 480 Argentine municipalities stood at US$913.8 million, equivalent to 33.6% of their annual revenues (23.5% of it being funded debt and 10.1% floating debt). This compares favorably with the provincial debt picture: the debt stock of 14 of the

23 provinces that year exceeded 50% of their total annual expenditure. However, the short-term profile of this debt (45.3% of it matures in one year or less) has had negative fiscal effects on the municipalities, such as the growing earmarking of their share-out receipts, the need for short-term refinancings, and the rising cost of the associated debt service.

1.12 As for creditor and term profiles, the debt stock of these representative municipalities breaks down as follows: (a) 80% is documented debt, of which: (i) 43% is owed to government agencies (utility-payment arrears, pension and social-fund contributions), half of it short-term obligations (1 year) and the other half at medium term (10 years); and (ii) 57% is owed to private companies, mainly banks (predominantly medium-term borrowings) and private companies (predominantly short-term); and (b) 20% is undocumented government and private-sector debt, with no refinancing term, such as amounts outstanding to suppliers and payroll arrears. The maturity breakdown for the aggregate debt of these municipalities is: (i) 43%, maturities of one year or less; (ii) 14%, up to five years; (iii) 32%, up to 10 years; and (iv) 11%, longer than 10 years.

1.13 As for the distribution of the debt by repayment term and size of municipality, the small and mid-sized municipalities in the sample (up to 100,000 population) account for about 70% of aggregate municipal indebtedness and for 80% and 92% of short-term and medium-term municipal debt, respectively. Table I-5 illustrates this breakdown.

Table I-5
Breakdown of debt by term and municipality size, 1997

<table>
<tr><th>Size (population)</th><th>Up to 1 year</th><th>5 years</th><th>10 years</th><th>Over 10 years</th></tr>
<tr><td>Up to 10,000</td><td rowspan="4">84%</td><td rowspan="3">92%</td><td rowspan="5">80%</td><td rowspan="3">87%</td></tr>
<tr><td>10,001 – 50,000</td></tr>
<tr><td>50,001 – 100,000</td></tr>
<tr><td>100,001 – 150,000</td><td rowspan="3">8%</td><td rowspan="3">13%</td></tr>
<tr><td>150,001 – 250,000</td><td rowspan="2">16%</td></tr>
<tr><td>Over 250,000</td><td>20%</td></tr>
<tr><td>TOTAL</td><td>100%</td><td>100%</td><td>100%</td><td>100%</td></tr>
</table>

1.14 In the breakdown of total average debt by municipality size, the former rises steadily until the 250,000-population level. The reverse is true for mid-sized municipalities (10,000 – 150,000

population) when extreme values of per capita debt are compared (from 288 pesos down to 70 pesos), as Table I-6 illustrates.

Table I-6
Average debt by municipality size, 1997

Size (population)	Total (thousands of pesos)	Per capita (pesos)
Up to 10,000	500	Up to 53.7
10,001 – 50,000	2,900	288 to 58
50,001 – 100,000	7,000	140 to 70
100,001 – 150,000	10,500	105 to 70
150,001 – 250,000	25,600	171 to 103
Over 250,000	15,900	64 or less

1.15 The evident conclusion is that the debt situation of municipalities with populations of 100,000 and under is more critical than in their larger counterparts. This has been taken into account in scaling the program proposed herein, in which an estimated 68% of the total financing would be absorbed by municipalities with populations up to 100,000 (see chapter IV). As further backing for this approach, 134 (91%) of a universe of 147 municipalities that have expressed serious interest in the program have populations of 100,000 and under.

5. Main institutional and municipal-management problems

1.16 The problems with which Argentina's municipalities are having to grapple fall into three broad areas: (i) administrative management, organization, and planning; (ii) revenue management; and (iii) financial management. Table I-7 summarizes the problems of greatest concern in each of these areas that are facing a representative sample of 480 municipalities.

a. Administrative management, organization, and planning problems

1.17 The administrative management model in use in Argentine municipalities suffers from weak internal administrative procedures. Tender calls and routine applications for building permits and business licenses, for instance, are unduly complicated and take far too long to arrange. These shortcomings can be attributed in large measure to a lack of organizational structures concordant with the functions falling to each unit in the municipal

apparatus. An estimated 75% of municipalities have no organization or functions manuals; an even higher percentage have never cleared their partial organizational adjustments with their town councils. For the most part municipalities are relying on provincial audit offices for internal control tasks because municipal control systems are so behind the times.

Table I-7
Main institutional problems of municipalities

1. **Administrative management, organization, and planning**

- 80% of the municipalities have no official, current organization chart. Some have adjusted their structures but the changes have not been cleared by the respective town council.
- 75% of the municipalities have no organization, functions, or procedures manuals, and their staff has no specifically assigned functions or responsibilities.
- Internal control systems in 66% of the municipalities are out of date; provincial audit offices are performing some control functions.
- 90% of the municipalities have no strategic plan, public works master plan, or other formal planning instrument in place.
- There is no merit-based promotion arrangement or systematic training in any of the municipalities' human resources management systems.
- The information systems in 80% of the municipalities are not integrated and have no security features.

2. **Revenue management**

- 90% of the municipal tax systems take in a wide array of taxes, making collection difficult. Furthermore, some municipal regulations and tax bases are not compatible with their provincial counterparts.
- 95% of the municipalities have no master taxpayer roll or current-account system.
- There are no systematic compliance monitoring and audit plans, only isolated checks, in only 5% of the municipalities.
- Though municipalities have enforced-collection powers, in practice less than 10% of them exercise this authority.
- Property rolls and property values on record are out of date in virtually all the municipalities.

3. **Financial management**

- In 85% of the municipalities, financial management systems have been computerized but not integrated.
- Budget systems in 90% of the municipalities are not directly compatible with those of the respective province or of the federal government, making it difficult to consolidate information.
- In 87% of the municipalities, public investment systems are not aligned with the national law governing the federal system in this regard.

1.18 Some 90% of municipal governments have virtually no current urban development plans, public works master plans, or investment systems to underpin planned, orderly municipal growth. Two main reasons for this state of affairs are the municipalities' ineffectual information systems and the lack of training and development for municipal employees, in both management and operations areas. Overall, human resources management in the municipalities is not built around systematic training programs or possibilities of merit-based advancement.

1.19 The municipalities are also ill-equipped on the physical side, with inadequate, if not obsolete, hardware and software. One serious

problem is the lack of security features in the information systems of nearly 80% of the municipalities.

1.20 Municipal service delivery in a number of sectors is not up to standard. The weaknesses are evident in such areas as street cleaning and lighting, city maintenance and roads, which present problems in organization, service coverage, and equipment and infrastructure, among others. Furthermore, there are few mechanisms for publicizing services and assistance available to the public, and those that do exist are haphazard. In general, the community has little say in the workings of its municipal government because with few exceptions government operations are closed to the citizenry: information on budget execution, for instance, is publicly available in only a handful of municipalities, and few have devised any avenues for public consultation.

b. Revenue management problems

1.21 The municipalities have trouble generating own revenues, in part because of inadequate tax legislation and in part owing to functional problems in their revenue bureaus. As for the first of those problems, municipal tax codes do little to expedite tax management, including as they do too many small-yielding levies which are complicated to administer. In some municipalities, municipal tax legislation is not even compatible with provincial laws — for instance, in defining certain tax bases. Likewise, 95% of municipalities have no master tax roll and collection systems (such as current-account systems that can furnish aggregated data on the tax liability of each taxpayer).

1.22 The second problem, the functional makeup of municipal revenue bureaus, makes it difficult for these local governments to collect taxes efficiently. For one thing, few of them have compliance monitoring and audit units or plans, and only about 5% do tax inspections and audits. Very few exercise their enforcement authority. Other serious constraints are out-of-date property rolls and the fact that property data are spread among various records offices, making for less than efficacious tax collection.

c. Financial management problems

1.23 The municipalities do not have integrated information systems for financial management, which would expedite budget management and efficient tracking of municipal spending. The financial management modules in place for budgeting, accounting, cash management, and procurement and contracting are not integrated; fully 90% of the municipalities have budget systems incompatible with the national and provincial government systems. Since budget classifiers, for instance, are not grounded in technical criteria, it is difficult to compare accounting and financial information across municipalities; nor is there uniformity between municipal and

federal public investment systems. In virtually no municipality are financial management systems directly linked in to tax administration systems.

B. The federal government's strategy for the sector

1. Provincial fiscal reform and municipal decentralization 3/

Table I-8
The Federal Fiscal Pact

The Federal Fiscal Pact is a policy instrument worked out between the national government and the provincial governments for the implementation of provincial structural reforms such as: (i) strengthening the provinces' capacity to generate own resources; (ii) modernization of the provincial civil service; (iii) abolishment of inefficient taxes; (iv) deregulation of provincial economies; and (v) transfer of provincial employee pension funds to the national pension plan. Two such Pacts have been framed thus far, the first in 1992 and the second in August 1993, which remains in effect. This second accord sets out municipal fiscal reforms comparable to those already adopted at the provincial level.

1.24 Fiscal reform in Argentina's provinces began early in the 1990s with the adoption of the Federal Fiscal Pact (see Table I-8), which was intended to right the provinces' most serious structural financial imbalances and better equip them to generate current savings. This paved the way for a rethinking of federal-provincial financial relations and for better-defined and shared responsibilities for government service delivery. Between 1991 and 1997, consolidated figures for the provinces (including the City of Buenos Aires) point to improvements in fiscal performance markers, such as a 74.4% increase in provincially collected tax revenues and a 60.7% reduction in the fiscal deficit.

1.25 With regard to municipal development policy, the federal government intends to push for application of the principles set out in the Federal Fiscal Pact, particularly to redefine what revenues municipalities can collect and expend independently, to review revenue-sharing arrangements, and to purge and streamline obsolete and unnecessary regulations. The main change for the municipalities on the taxation front will be the abolishment of municipal levies that do not represent payment for an actual service rendered or exceed the cost associated with the service.

1.26 To put this policy into practice, the federal government proposes to foster a series of municipal government reforms, to put

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3/ Within the framework of the current Federal Fiscal Pact, the Bank and the World Bank will support revenue-sharing reforms under the special structural adjustment and strengthening of banking system safeguards program (AR-0254). This program calls for putting in place simplified and more equitable rules for primary and secondary distribution of revenue share-outs to provinces and municipalities. These measures will bolster the viability of the municipal reforms planned under the program.

municipalities' finances in order and strengthen their institutional workings. The focus of this effort will be to: (i) rewrite municipal tax codes and strengthen municipal tax administrations; (ii) align financial management systems with the National Financial Administration Act and bring in efficient management systems; (iii) give the municipalities modern financing structures for investments and city services; (iv) institute municipal information systems compatible with the provincial ones; and (v) streamline municipal spending.

2. Restructuring of municipal debt

1.27 The national government has at its disposal resources from the Fund for Provincial and Municipal Public Sector Reform, which it proposes to use to refinance the municipalities' debt. It has established strict conditions for such operations, which would be tied to compliance with eligibility conditions for the program to be funded by the Bank. These include adoption of a Reform and Investment Plan (PRI) setting out targets for the commitment to balance the fiscal accounts and boost current savings, among others. The sequence of disbursement of Fund monies to municipalities taking part in the proposed program would be as follows: (i) 30% upon signature of a program participation agreement, clearance of the PRIs by the Central Executing Unit (CEU), and authorization to borrow from the program proceeds; (ii) 20% upon CEU clearance of final reform-project proposals submitted by the municipalities and signature of subsidiary loan agreements; and (iii) the 50% balance when the reform projects in the approved PRIs are awarded. The municipalities' debts would be refinanced over a period of up to 10 years, at interest of between 8.75% to 10% inclusive, with a grace period of up to six months.

3. Program strategy

1.28 Argentina's institutional experience with subnational government operations suggests that the best way of improving fiscal and administrative management practices is to combine incentives with clear guidelines as to pursuable targets. The program's strategy will be to link incentives – financing for priority investments, and rescheduling of short-term debt of the municipalities most in need – to requirements for institutional reforms and the attainment of clearly defined fiscal targets. This is a technically sound approach, based as it is on reform target-setting on the strength of systematic diagnostic assessments for each municipality, so as to design workable programs agreed upon with the municipalities. Progress toward these targets and in these programs would be reviewed yearly to make certain they are being properly implemented, to ultimately bring about the changes the program is seeking (see paragraph 3.36).

1.29 This strategy is instrumental for achieving the efficiency gains to which decentralization opens the door. The program would help move

forward the kind of management reforms that will be essential for deeper decentralization and for giving municipalities' readier access to private investment funding. Furthermore, the program is an essential intermediate step between the current municipal finance model and one that can tap into private savings. The program therefore calls for activities to expedite access to that kind of financing which, if duly supervised, can help instill greater fiscal discipline in municipalities benefiting from the program.

C. The Bank's strategy and rationale for its involvement

1.30 The Bank's strategy for its operations with Argentina calls for support for three core areas of action: (i) poverty reduction and improving the quality of life of Argentina's people, by creating employment and expanding coverage of basic services; (ii) raising productivity and heightening competition in domestic production; and (iii) deepening and consolidating reforms of the State and extending such modernization efforts to the provinces and municipalities.

1.31 The program proposed here fits within the aforementioned strategy inasmuch as it will support tax, financial, and institutional reforms, to help assure fiscal and financial sustainability of the country's municipalities along with adequate coverage and quality of municipal services. More specifically, the program will afford support to the federal government in implementing its strategy to see the Federal Fiscal Pact adopted in the country's municipalities.

D. Experience of the Bank and other lending agencies in the sector

1.32 The Bank's first operation in Argentina's urban-municipal sector dates back to 1962. Thus far it has approved eight loans to that sector totaling US$743.2 million. The following paragraphs summarize the objectives and status of the Bank's four most recent loans to this sector.

1.33 The global urban development program (loans 206/IC-AR and 514/OC-AR totaling US$122 million, signed in 1987) sought to improve the quality of life of urban residents and give them better access to municipal services. It funded infrastructure construction and city equipment, with backing from associated technical assistance projects. These loans have been disbursed in full and the program has been completed.

1.34 Loans 830/OC-AR and 932/SF-AR, signed in 1995, provided US$210 million in funding for a program for institutional development and municipal social investments. The objective of that program was to assist the municipalities in their efforts to improve the quality of life of their residents, particularly those of fewest means, and to support the national government with its

decentralization and public-finance rehabilitation program. The program is now well under way, operating in 14 of the country's 23 provinces. Practically all the loan proceeds have been committed, and 32% has been disbursed.

1.35 These programs effectively rose to the municipalities' demands for technical assistance and investment. They left the subexecuting agencies (provinces and/or municipalities) with project development and procurement procedures in place and thereby substantially strengthened their institutional apparatus, in some cases with backing from specific institution-building projects. The experience with delegation of responsibility for project approval and procurement was positive; it stimulated the strengthening of these capabilities among municipal technical officials.

1.36 In 1998 the contract for loan 1068/OC-AR for US$260 million was signed, to fund a comprehensive development program for large urban agglomerations in the interior. This program will benefit the five largest urban population centers in the interior, which have grown up around the cities of Córdoba, La Plata, Mendoza, Rosario, and Tucumán. It will help implement regional projects and foster institutional reforms in municipalities in those parts of the country. Disbursements have not yet begun, owing to the unexceptional difficulty of satisfying conditions precedent when a consensus first needs to be worked out between legislative bodies of the municipalities in each large urban area, to be eligible for the program's funds.

1.37 Through these projects, the Bank has helped create the capacity to carry out investment projects at the local level. Support for the national government's policy of decentralization, restructuring of municipal finance, and institutional reform fall under an area of recent experience now under way. In cases where provincial and municipal approval of indebtedness legislation have been needed, time frames have been quite long, as indicated for large conglomerations.

II. THE PROGRAM

A. Objectives

2.1 The program's primary objective is to set in place institutional conditions for self-sustaining development of Argentina's municipalities. Its specific objectives are: (i) to afford incentives for sound financial management in municipalities; (ii) to make for more efficient and better-managed local government service delivery; and (iii) to strengthen instruments for funding local investment projects.

2.2 The specific objectives of the program are as follows:

a. Promote sustainable fiscal-account balancing in the municipalities by boosting their revenues, reducing spending, and tightening expenditure controls.

b. Raise the efficiency of local government services and social service delivery, improving the management of these services and creating conditions under which they can be concessioned out or privatized.

c. Improve investment programming and fund priority municipal investment projects.

d. Endow municipal governments with modern internal administration systems, and train municipal human resources.

e. Support the creation of financing mechanisms whereby municipalities can look to the capital market for medium- and long-term funding to finance their investment projects.

B. Program components

2.3 The starting point for the program will be negotiations with participating municipalities on Reform and Investment Plans (PRIs), which will set out fiscal adjustment targets to which the municipalities will commit, and institutional reforms and investment projects that the program will finance. In keeping with those plans the program will fund the following components:

1. Municipal reforms component (US$200 million)

2.4 This component will fund the development and implementation of modernization and institution-strengthening projects to improve municipal finances and management. It will bring in computer systems, upgrade policies and regulations, and train human resources to operate the new systems. Priority will be given to reforms in tax administration and financial management, and to

setting up property records offices. The main activities to be funded are:

a. Financial management and tax administration, including: (i) strengthening of municipal tax-collection capacity and tax management; (ii) development and implementation of integrated financial management systems taking in, for example, budgeting, accounting, cash management, procurement and contracting; and (iii) updating and modernizing property rolls, with an emphasis on aligning municipal and provincial systems.

b. Internal administration and efficiency of government services. This strengthening of internal administrative arrangements will encompass: (i) improvements in management of the chief municipal government services (street cleaning, road maintenance, social services, etc.), including assistance in devising concession and privatization schemes; (ii) streamlining the human resources sector; (iii) support for planning, investment programming, and project preparation; and (iv) support to prepare computer systems to deal with the year 2000 problem.

2.5 The reform projects will be commissioned on the basis of outputs or systems installed and operating, including training for municipal employees and systems maintenance, where applicable, for at least one year.

2. Investment component (US$277 million)

2.6 This component will finance investment projects that are priorities for the municipalities' socioeconomic advancement. Eligible sectors are: (i) city and rural roads; (ii) storm drains and erosion and flood control structures; (iii) social services such as preschool facilities, seniors' homes, and community centers; (iv) city services such as trash collection and disposal, street lighting, and transit terminals; and (v) environmental protection, parks and other green spaces, among others.

2.7 Investment projects will be devised by reference to priorities substantiated in local development plans and sector master plans. Projects will have to satisfy specific economic, technical, financial, and environmental criteria, set out in the Operating Regulations and the project preparation guidelines. It will also have to be shown that they are not duplicating other sources of financing.

3. Municipal private borrowing component (US$2 million)

2.8 This component will help institute a sustainable private financing process for municipal projects. To that end the program will fund the following studies:

a. Studies to develop financing mechanisms that can **give municipalities access to the capital market**, focusing on: (i) legal and operational viability of mechanisms aimed at broadening municipal access to the markets, including an analysis of security options (based on revenue share-outs and miscellaneous assets), securitization of municipal bonds, and trusts to administer security, among others; (ii) ways of broadening municipalities' access to the securities market (which does operate now, but at very high interest rates), examining ways of making municipalities more competitive, such as auctions of municipal securities and/or competitive bidding by financial institutions for such intermediation business; and (iii) a model contract for municipal securities issues that can be adapted to operations with similar features. The studies should also produce concrete operational proposals of financing schemes, which will be developed as the final stage of the studies. Funding also will be available for technical assistance to track implementation of the proposals, which can become pilot municipal securities offerings.

b. Informational activities: (i) a study to systematize information on legal and accounting requirements for debt securities offerings and collateral, and on the regulatory role of the National Securities Commission; (ii) a model for municipal financial market reporting, with reference to revenue-sharing arrangements in each province and each municipality's commitment as to the revenue share-out; and (iii) training seminars for municipal leaders and technical teams, so they can fully understand how the capital market works and different avenues for tapping it.

C. Reform and Investment Plans and sequencing of the program

2.9 The program will pursue objectives that have been worked out with each municipality, by providing funding for reforms and investments. The technical conditions for these agreements with municipalities will be set out in Reform and Investment Plans (PRIs). The municipal diagnostic assessments contained in these plans will be the basis for setting project priorities. They will be organized into three modules: (i) a financial module containing financial projections for the municipality, information on its fiscal weak points, and anticipated impact of the proposed adjustment measures, projects, and reforms, with annual targets; (ii) a management and reforms module setting out the most serious problems besetting administrative systems and management of municipal services, and requirements for institutional reforms and projects to enhance the management of administrative systems and external services; and (iii) an investment module setting out the municipality's investment priorities, by reference to its sectoral and socioeconomic problems. A technical analysis of the reform and investment projects is to be appended to the PRI.

2.10 PRIs will be drawn up by consultants hired by the Central Executing Unit. The associated projects and fiscal targets will be discussed and agreed on with the municipal authorities. The first step in carrying through a PRI will be the execution of reform projects. Once it is demonstrated that those projects are duly under way, program funds can be released for investment projects (see paragraph 2.11). Progress on the reform and investment projects will be reviewed each year against the targets in the PRI in question (see paragraph 3.36). Reform-project execution will be monitored using a system of performance benchmarks and impact indicators, to be able to compare the municipalities' performance and attainment of the program's development objectives as set out in the logical framework (see Annex II-1).

D. Eligibility criteria

2.11 The program will be open to any Argentine municipality which (a) pledges to carry through institutional and administrative reforms; (b) is creditworthy, and (c) demonstrates that it can, by way of the program, balance or improve its fiscal accounts. To receive funds to carry out investment projects, a municipality must have begun, at least, the reform projects to improve financial management and tax administration agreed on for year 1, and show that they are proceeding satisfactorily.

E. Ceilings by municipality

2.12 The ceilings on program funds that can be made available to individual municipalities will be determined by reference to population ranges. The ceilings have been set to be able to support as many municipalities as possible, in the different population ranges, on the basis of average cost of the reforms in each type of municipality. A measure of flexibility could be allowed in the ceilings where financing is intended exclusively for reforms that call for extraordinary investment outlays and will produce fiscal improvements in future. Table II-1 shows the cost of each funding category.

Table II-1
Funding ceiling by size of municipality

Size of municipality (population)	Funding ceiling (US$000)
Under 10,000	1,000
10,000 - 50,000	2,000
50,000 - 100,000	2,500
Over 100,000	3,000

F. Cost and financing of the program

2.13 The estimated total cost of the program is US$500 million, to be funded by way of a US$250 million loan from the Bank's ordinary-capital Single Currency Facility and a US$250 million counterpart contribution from the Argentine Nation.

Table II-2
Total program cost and financing
(millions of U.S. dollars)

Cost Item	IDB/OC	Local	Total	%
1. **Administration and supervision**	**9.5**	**9.0**	**18.5**	**3.7**
1.1 Central Executing Unit	**4.0**	**0.5**	**4.5**	**0.9**
1.1.1 Consulting services	4.0	0.5	4.5	
1.2 Local implementation support	**5.5**	**8.5**	**14.0**	**2.8**
1.2.1 Consulting services	5.5	8.5	14.0	
2. **Components**	**238.0**	**241.0**	**479.0**	**95.8**
2.1 Reform projects	**100.0**	**100.0**	**200.0**	**40.0**
2.1.1 Consulting services	75.0	75.0	150.0	
2.1.2 Equipment	15.0	15.0	30.0	
2.1.3 Construction and furnishings	10.0	10.0	20.0	
2.2 Investment projects	**136.0**	**141.0**	**277.0**	**55.4**
2.2.1 Design	2.0	2.0	4.0	
2.2.2 Construction	134.0	139.0	273.0	
2.3 Municipal private borrowing	**2.0**	–	**2.0**	**0.4**
2.3.1 Consulting services	1.7	-	1.7	
2.3.2 Training	0.3	-	0.3	
3. **Financial charges**	**2.5**	–	**2.5**	**0.5**
3.1 Inspection and supervision	2.5	–	2.5	0.5
TOTAL	**250.0**	**250.0**	**500.0**	**100%**
Percentage	**50%**	**50%**	**100%**	

III. PROGRAM IMPLEMENTATION

A. The borrower

3.1 The borrower will be the Argentine Nation, which will appoint the Ministry of the Interior (MINTER) as executing agency. MINTER will implement the program by way of its Office of Financial Assistance for the Provinces. The Central Executing Unit (CEU) in that Office will coordinate the program activities.

B. Executing agencies

1. Central Executing Unit of the Ministry of the Interior

3.2 The CEU is already implementing IDB and World Bank projects in the area of subnational management, and has the capacity and experience to carry through this new operation. At this writing it is responsible for nine IDB- and World Bank-funded programs involving aggregate financing of US$2.82 billion. 4/ Under its matrix-type internal organization each program is coordinated by one official, with support from sectoral management and technical/administrative areas. The sectoral management area deals with questions of infrastructure, contracting, fiscal affairs, systems, and legal matters for all the projects being supervised. The technical/administrative area takes in administration and finance per se, central reception, the roster of consultants, and information systems and databases. The CEU organization chart is presented in Annex III-1.

3.3 For the proposed program, an additional division would be set up within the CEU, in the subnational management area, under the supervision of the Deputy Executive Coordinator, which will coordinate its work with the current sectoral management area with support from the technical/administrative area. The CEU's staffing would be progressively bolstered by additional personnel in areas in which the incremental workload could not be absorbed by current staff. This is expected to mean an additional 18 employees to strengthen (in principle) the fiscal affairs, environmental, infrastructure, contracting, accounting/administration, and project analysis areas. This configuration will take advantage of CEU installed capacity, to avoid overlapping of tasks and overstaffing.

4/ Since the CEU's experience under three of these programs relates to financial and fiscal restructuring, technical assistance, and investments associated with the provinces, it is considered to have sufficient capacity to execute this new operation with municipalities.

3.4 The CEU will also be in charge of administration, coordination, supervision, and evaluation of the proposed program and of dealings with the Bank.

3.5 To formalize the CEU as executing unit for this new program and give it the requisite legal authority, the borrower, as a condition precedent to disbursement of the loan, **must demonstrate to the Bank's satisfaction that it has formally placed the CEU in charge of the program's implementation.**

2. The municipalities

3.6 To support local execution of the projects, the CEU will contract consulting services for administrative work, to guide or perform accounting and administrative tasks for the program, as well as monitor implementation of the projects and train municipal personnel.

3.7 **As a special condition for the loan, within six months after the effective date of the loan contract the CEU would have to demonstrate that it had engaged sufficient consulting firms for supervising, in proportion to the municipalities already included to the Bank's satisfaction, operations planned for year 1 of the program.**

3.8 The municipalities will be required to present annual budget outturn reports countersigned by the municipal executive, and financial statements for the program, audited by independent public accountants.

C. Agreements required

3.9 The following legal instruments would be needed for implementation of the proposed program.

1. Program participation agreement

3.10 A prerequisite for a municipality to join the program will be the execution of a program participation agreement. This instrument will spell out the program objectives, components eligible for funding, and the possibility of the municipality's refinancing its debt by way of the Fund for Provincial and Municipal Public Sector Reform (such operations not being part of the program). The agreement will likewise stipulate conditions for the municipality to qualify for program funds and the tie-in between compliance with these conditions and release of funds to refinance its debt.

2. Subsidiary loan agreement

3.11 The national government will onlend the proceeds of the loan to the municipalities by virtue of subsidiary loan agreements,

corresponding to the programs agreed on in the respective Reform and Investment Plans, with specific annexes pertaining to each project to be funded. These agreements are to be backed by the province in question as evidenced in guarantee agreements, and must be accompanied by the following:

a. Municipal ordinances authorizing: (i) borrowing by the municipality, and (ii) assignment of federal revenue share-outs as a guarantee of the local counterpart resources and principal and interest payments on the loans.

b. Studies, bid documents, and other documents showing that the reform and construction projects for which program funds are being sought satisfy the eligibility requirements in the program's Operating Regulations.

c. Project completion and funding timetables, and timetables for implementing the reforms.

d. Targets to be achieved in implementing the reforms set out in the respective Reform and Investment Plan.

3. Guarantee agreement

3.12 A guarantee agreement will be executed between the national government, the province in which a participating municipality is located, and the participating municipality, pledging revenue share-outs as security for repayment of the loan and furnishing of the counterpart falling to each municipality.

D. Allocation of program funds

3.13 The program funds will be allotted in order of signature of participation agreements. If, because of lighter-than-anticipated demand, all the funds have not been apportioned by the end of year 2, consideration will be given to approving additional loans to municipalities that have already taken part in the program, provided they are meeting the fiscal adjustment targets in their Reform and Investment Plans (see paragraph 3.36) and have completed their reform projects as planned. Such additional loans would be bound by the same ceilings set for the initial allocation; funding would be approved in order of the municipalities' applications.

3.14 Subsidiary loan agreements will stipulate the deadline for commitment and disbursement of the proceeds of the loan to each municipality, not to exceed one year (for the municipal reforms component) and two and one-half years after signing, respectively.

E. Transparency

3.15 The following guidelines have been established to ensure adequate transparency in the use of program funds:

(a) The executing agency is to distribute a copy of the Operating Regulations to all the municipalities in the country within sixty (60) days after the loan contract effective date (see paragraph 3.29);

(b) The CEU is to keep a record of requests received from municipalities wishing to join the program. Registering municipalities will receive a number based on order of receipt, and the record is to be available to all municipalities. Those who so require may request a formal review of their program status from the CEU, with a copy to the Bank; and

(c) The executing agency is to distribute each year during the program, to all the country's municipalities with a copy to the Bank, an annual report covering activities carried out since the program's outset, with statistical highlights (list of municipalities implementing projects; number, type and amount of reform and investment projects; amounts committed and disbursed; physical progress on projects; etc.).

F. Terms and conditions for onlending the loan proceeds

3.16 The borrower will onlend the loan proceeds to the municipalities by way of subsidiary loan agreements, on terms similar to those of the loan.

G. The project cycle

1. Eligibility determination and preparation of Reform and Investment Plans

3.17 The project cycle is initiated by a request from a municipality to take part in the project. For a municipality to be eligible, it must:

a. pledge to carry through institutional and administrative reforms;
b. be creditworthy; and
c. show that, by implementing the proposed project, it can balance or improve its fiscal accounts.

3.18 After assessing the application the Central Executing Unit (CEU) sets a borrowing ceiling for the municipality and decides on the scale of fiscal adjustment required.

3.19 Once a municipality is declared eligible, with support from consultants it puts together financial, institutional, sectoral, and environmental diagnostic assessments and its reform projects and investment profiles, and sets financial targets for the proposed fiscal adjustment measures and its debt-refinancing requirements. This package of information constitutes the municipality's Reform and Investment Plan (PRI).

2. CEU assessment

3.20 The CEU examines each PRI and the targets, profiles, and projects set out therein; if the PRI's content is satisfactory, the CEU clears the plan. Approval of a PRI does not, however, mean approval of the individual projects described in it; that will depend on an evaluation of working designs that have to be submitted as a condition precedent for projects to be funded. When a PRI has been approved, the municipality is invited to sign a program participation agreement.

3.21 Once the CEU has approved the above-mentioned documents, the municipality must present the municipal ordinance that authorizes it to borrow, and a provincial guarantee, backed by tax revenue share-outs, is furnished by the province in which the municipality is located.

3.22 Where necessary, and in accordance with the approved PRI, the national government and the municipality will execute a debt refinancing agreement, whereupon up to 30% of the amount of such refinancing can be released.

3.23 Once the foregoing stages are completed, the municipality can execute a subsidiary loan agreement with the federal government for the agreed loan amount.

3. Project development and implementation

3.24 The first stage in the operation of a subsidiary loan agreement are the municipality's **reform projects**. To receive program funds for its **investment projects** the municipality must have begun and show satisfactory progress on at least the tax administration and financial management reform projects agreed upon for year 1. The municipality completes the working designs for the investment project, with the help of consultants if needed, and sends the documentation to the CEU for review.

3.25 For investment projects, the CEU appraises the proposed projects by reference to selected technical, economic, financial, and environmental criteria, which apply to every investment sector. When it has cleared a project it forwards the information to the Bank (or notifies the Bank, if so provided) to secure its non-objection. Any projects not cleared are sent back to the municipalities to be reworked or replaced. The municipalities produce bid documents, call for tenders, and forward to the CEU the bid evaluation report and their recommendation for the contract award.

3.26 With support from the CEU, the municipality contracts with the supplier or construction firm, and the reform or investment project begins.

3.27 The PRI targets are reviewed each year (financial, fiscal, and for reform and investment project implementation).

3.28 The reports that the CEU is to produce periodically for the annual reviews of the proposed program will include a summary report on the status of PRI implementation.

H. Implementation arrangements

3.29 The program will be executed in accordance with the operational, technical, financial, and environmental requirements, rules and procedures set out in: (i) the loan contract covenants and (ii) the program's Operating Regulations (**entry into force of the Operating Regulations will be a condition precedent for the first disbursement of program funds**). Other prerequisites for the first disbursement are: (i) **presentation, to the Bank's satisfaction, of the final PRI model**; (ii) **execution of 15 subsidiary loan agreements between the borrower and municipalities eligible for the program**; and (iii) **opening of a special account with the Fiscal Agent to receive disbursements of program funds**.

3.30 The following will be special conditions in the loan contract: (i) **within 90 days after the effective date of the loan contract the executing agency must demonstrate that it has distributed a copy of the program's Operating Regulations and additional pertinent information to all municipalities in Argentina**; and (ii) **as a condition for disbursements under the municipal private borrowing component, the executing agency must present, to the Bank's satisfaction, terms of reference of the studies to be commissioned**.

3.31 No funds may be disbursed for a municipality until the set of agreements evidencing approval of the respective reform or investment project have been formally executed.

I. Inspection and supervision of works

3.32 Where necessary for inspection and supervision of works projects (including environmental elements), specialized consultants or consulting firms will be hired.

J. Cost-recovery mechanisms

3.33 Capital outlays for investment projects and their operating, administrative, and maintenance costs will be recovered through general and specific taxes, betterment levies, and municipal rates. Where clear identification of a project's beneficiaries is impossible or not warranted, cost recovery will be by way of the municipality's general revenues, provided this does not run counter to the program's objective of balancing or improving the fiscal accounts.

K. Monitoring of the program (discretionary limits)

3.34 The CEU may approve PRIs and reform and investment projects without prior clearance from the IDB. The Bank will perform ex post sampling checks of CEU approvals (but will do ex ante reviews of the first 15 PRIs).

3.35 The borrower, through the CEU, will provide the Bank with semiannual progress reports on the program, within 30 days after the end of each calendar half-year until the program is completed.

3.36 The executing agency and the Bank will meet yearly to review progress on the program, adherence to the implementation requirements and arrangements referred to earlier, and compliance with the indicators specified in the logical framework.

L. Disbursement periods

3.37 The program funds will be disbursed over five years, calculated from the effective date of the loan contract.

M. Procurement procedure and timetable

3.38 When the loan proceeds are to be used, international competitive bidding will be mandatory for purchases of goods worth US$350,000 equivalent and up and for construction contracts of US$5 million equivalent or more.

3.39 The Bank will do ex post sampling checks of procurements of goods costing less than US$350,000 equivalent and construction contracts under US$5 million equivalent.

3.40 International competitive bidding will be required to engage consultants on contracts of over US$200,000 equivalent. The Bank will do ex post sampling checks of consulting-firm contracts worth less than US$200,000 equivalent and individual-consultant contracts below US$50,000.

3.41 The foregoing notwithstanding, when the Central Executing Unit is acting for the first time at any procurement stage (whatever the sum involved) it must seek clearance from the Bank for every such stage (procurement of construction work, goods, consulting firms, individual consultants).

3.42 The procurement timetable will be worked out semiannually, as municipalities file their loan applications. The procurement schedule is included in Annex III-2, and the following table gives a tentative timetable for the program as a whole.

Table III-1
Tentative procurement timetable
(thousands of U.S. dollars)

	Year 1	Year 2	Year 3	Year 4	Year 5	Total
Annual disbursements	75,000	125,000	150,000	100,000	50,000	500,000
% of total	15%	25%	30%	20%	10%	100%

N. Revolving fund

3.43 It is proposed that a revolving fund equivalent to 5% of the loan be set up to defray program expenses.

O. Audits

3.44 The borrower is to provide the Bank with annual financial statements for the program, accompanied by the opinion of an independent external audit firm.

3.45 Each year, municipalities taking part in the program must present their budget outturn reports countersigned by the municipal executive.

P. Program readiness

3.46 A sample of nine PRIs from nine municipalities are already at hand, and the CEU has preliminary information for the preparation of a further 110 such plans. This would assure activities for year 1 of the program.

Q. Ex post evaluation

3.47 No ex post evaluation of the program is planned. Should the borrower or the Bank decide to conduct such an evaluation, however, the requisite information will be available in the program monitoring reports.

IV. PROGRAM VIABILITY AND RISKS

A. Viability

1. Analysis of the sample

4.1 The mission reviewed the scale of the program by reference to an analysis of average cost of the reform and investment projects examined on the basis of Reform and Investment Plans (PRIs) for an indicative sample of nine municipalities (see paragraph 4.2), projecting these costs over an estimated demand of 300 municipalities belonging to the representative sample of 480 Argentine municipalities used in the diagnostic assessment in chapter I. From this exercise it was concluded that 41.9% of the total program cost would be for reform projects and 58.1% for investment projects. 5/

Table IV-1
Sizing of the program
(thousands of U.S. dollars)

Size of municipality (population)	Number of munici-palities	Average cost		Total cost		TOTAL
		Reform	Investment	Reform	Investment	
Under 10,000	154	400	600	61,600	92,400	154,000
10,000 — 50,000	105	790	1,230	82,900	129,090	211,990
50,000 — 100,000	24	1,250	1,250	30,000	30,010	60,010
Over 100,000	17	1,500	1,500	25,500	25,500	51,000
TOTAL	300	-	-	200,000	277,000	477,000
Percentage				41.9	58.1	100%

2. Viability of reform projects

4.2 The technical viability of reform projects was analyzed by reference to: (i) quality of the diagnostic assessment of the main institutional problems of an indicative sample of nine municipalities (see paragraph 4.9); (ii) suitability of the proposed project activities for addressing those problems; and (iii) proposed implementation arrangements. The diagnostic assessments are complete, and include an analysis of municipal ordinances and regulations, organizational structure of municipalities, their management, operations, and human resources management models, and their information systems. Each reform project envisages components and activities in line with the

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5/ The estimate of US$277 million for financing investment projects could be for full or partial financing.

diagnostic assessments; they focus on improving legal frameworks and developing new administrative, tax administration, and financial management systems, but also include instruments for expediting their implementation and evaluation and making them sustainable (see monitoring benchmarks provided in Annex II-1).

3. Viability of investment projects

4.3 The investment-project sample consisted of 23 projects that would cost a total of US$32 million, all of them in investment sectors eligible for the program. In each case the municipality had asserted its wish to join the program. Complete technical, economic, financial, and environmental feasibility analyses are at hand for 10 of the 23 projects with an aggregate cost of US$16.4 million. Since about 50 investment projects worth US$40 million in all could be contracted for in year 1, those 10 projects are enough to start off the program.

4.4 All of these projects have been appraised using project formulation methods agreed upon with the Bank and set out in the program's Operating Regulations, the analysis having looked at demand and least-cost alternatives. The above-mentioned 10 projects were found to be economically viable, affording economic internal rates of return higher than 12% and/or cost-efficient alternatives. Table IV-2 below summarizes the appraisal findings.

4. Institutional viability

4.5 According to the assessment done of the Central Executing Unit (CEU), including its organization, caliber of its professional staff and of their work and functions in the nine programs for which they are currently responsible (two with the IDB, seven with the World Bank), it has the requisite experience with international organizations in reform and investment project preparation and evaluation to be able to successfully implement and oversee the program proposed herein.

Table IV-2
Economic appraisal of the investment-projects sample
(thousands of U.S. dollars)

			Present value		
Sector/Project	**Municipality**	**Amount**	**Cost**	**Benefit**	**EIRR**
Storm drains	Resistencia	3,958	2,253	3,774	22.0%
Storm drains	Resistencia	1,385	1,141	1,220	13.0%
Roads/Paving (intercity)	Pocito	3,133	1,983	5,768	34.9%
Roads/Paving and street lighting	Marcos Juárez	2,028	1,446	3,661	24.4%
Roads/Paving and street lighting	C. Rivadavia	1,363	444	-	Least-cost alternative
Roads/Accesses	Trevelín	1,233	840	1,273	26.7%
Roads/Paving and street lighting	Puerto Madryn	2,497	1,378	-	Least-cost alternative
Roads/Maintenance	Rawson	540	419	-	29.0%
Environmental protection/Solid waste	San Francisco	811	378	606	15.0%
Parks and recreation	Resistencia	426	339	853	Least-cost alternative

4.6 The CEU would be given additional staff for this program. Consultants will need to be engaged to help the municipalities implement their reform projects, first to produce a PRI adhering to the methods agreed on by the Bank and the CEU, and then to develop and carry through specific projects. To that end, some CEU areas will be strengthened by bringing in experts in tax administration and sector specialists by province, who are familiar with the situation in the different municipalities. This will assure that the right consultants are hired and will make for sound technical appraisal and monitoring of projects.

4.7 It is estimated that an additional 18 professionals would be needed throughout the life of the program, at an incremental cost of about US$4.5 million over four years. The new employees would be recruited in areas in which the present staff could not absorb the incremental workload. In principle, three officers would be hired for fiscal affairs, two for the environmental area, two for infrastructure, two for procurement and contracting, two for accounting and administration, five with provincial sectoral expertise, and two in the program's executive office.

4.8 The municipalities – the program's beneficiaries, subborrowers, and coexecuting agencies – will receive needed support from the CEU directly or by way of consulting services to produce their PRIs and to develop and carry through their reform and investment projects. Relations between the CEU and the municipalities will be clearly

set out in the program participation agreements, subsidiary loan agreements, and the program's Operating Regulations. Each municipality's proposed reform and investment projects will be part of its PRI, and will be approved by the CEU.

5. Financial viability

4.9 The program's financial viability is contingent upon the viability of the Reform and Investment Plans. To illustrate the tie-in, such PRIs were prepared for each of the nine municipalities in the indicative sample. The following information was looked at: (i) the municipalities' financial performance over the past three years; (ii) the financial commitment represented by their total debt stock at present; (iii) details of the reform and investment projects they were proposing as an integral part of their PRIs; (iv) projections from the current situation showing the program's effect and the refinancing of short-term private borrowings as needed; and (v) each municipality's net budget outturn projection for 1998-2005 under three scenarios: (a) without the program (no PRIs); (b) with the program only (PRIs, no debt refinancing); and (c) with the program and concomitant debt refinancing plan (the PRIs per se). Table IV-3 illustrates the cumulative overall outcomes under each scenario.

Table IV-3
Cumulative outcomes 1/ 1998-2005
(thousands of U.S. dollars)

Municipality	Population	Current situation projected	Effect of the program	'With program' scenario	Effect of debt refinancing 2/	'With program + refinancing' scenario
Posadas	270,269	39,290	17,280	56,570	2,504	59,074
Huinca Renancó	9,474	4,982	851	5,833	943	6,776
Curuzú Cuatiá	35,333	(2,805)	2,576	(229)	3,223	2,994
Frontera	9,740	5,522	1,121	6,643	274	6,917
Reconquista	57,584	(937)	4,388	3,451	1,554	5,005
San Francisco	61,182	15,197	11,994	27,191	7,965	35,156
Jesús María	24,219	3,765	893	4,658	3,844	8,502
9 de julio	45,548	4,873	4,108	8,981	0	8,981
Trelew	101,674	5,708	3,074	8,782	1,881	11,663
SURPLUS		75,595	46,285	121,880	22,188	144,068

1/ Based on fund-flow projections for current and with-program municipal budget execution.
2/ Only short-term private borrowings of the municipalities will be eligible for refinancing; the resources will be drawn from the Fund for Provincial and Municipal Public Sector Reform.

4.10 As the table illustrates, the reform projects in the municipalities making up the indicative sample will benefit municipal finances,

supplying the equivalent of US$46.3 million in cumulative additional resources from 1998 to 2005. The refinancing of short-term private debt would make available a further US$22.2 million.

4.11 Conservative assumptions were used to project the reform operations' impact on the municipalities in the sample. In every case a detailed analysis was done of the growth factors utilized, and dates on which the improvements could be expected to be felt were adjusted. The result was the building in of a delayed-benefit factor, for the projections received, of from one to two years.

4.12 This shows that if PRIs are properly designed, municipalities receiving support under the program can produce enough revenues to balance their budgets (Curuzú Cuatiá and Reconquista), recover investment-project costs through the mechanisms instituted to that end, and pave the way for access to additional sources of private funding for their investment projects (see fiscal indicators in the logical framework attached as Annex II-1).

B. Environmental impact and environmental protection measures

4.13 An environmental impact assessment was prepared to gauge the program's environmental impact, pinpoint any foreseeable adverse effects, and ensure that the necessary mitigation measures would be adopted. The assessment report was released to the public on November 4, 1998. It looked at the following elements, among others: (i) an analysis of the sample of projects; (ii) environmental laws and the institutional framework for environmental protection; (iii) avenues for community involvement; (iv) environmental eligibility criteria; and (v) environmental monitoring and supervision procedures for physical investments, identifying the agencies responsible and their technical assistance needs in this regard.

4.14 The proposed program will improve the environmental balance for the population of each of the municipalities receiving funding, by virtue of: (i) the nature of the sectors that will be eligible, notably environmental protection and improvement and solid waste treatment and disposal; (ii) the building of environmental protection considerations into project development, implementation, and operation; and (iii) the establishment, in municipal governments, of environmental analysis methods as part of a comprehensive project design and development process, in some cases bolstering municipal environmental management capacity.

4.15 Any adverse effects that the projects might have on the environment during the construction period and thereafter are relatively slight and can be mitigated. This could include removal of plant cover, erosion, inconvenience to residents, and surface water and groundwater contamination. The environmental quality control procedures for the program take the form of: (i) the environmental impact assessment of the program; (ii) Appendix 1 to the Operating

Regulations for the program, including general and sector-specific environmental eligibility criteria; and (iii) the Project Development Guidelines. Recommendations in the environmental assessments of individual projects are to be included in the sets of bid documents for the respective construction work.

4.16 An environmental expert will help the CEU set up a workable environmental quality control sequence for the program. The municipalities, for their part, will have technical support to develop and supervise projects and to bring in environmental protection measures recommended in specific environmental assessments. The CEU will include a table in its annual reports to summarize: (i) environmental analyses of the projects and their preparation costs; (ii) community involvement; and (iii) environmental technical assistance actions and budget, among others.

C. Program benefits and risks

1. Benefits

4.17 The primary benefit of the program will be an increase in municipally generated revenues and more efficient use of those funds, thanks to the reform projects carried through in each municipality. The program also will help instill greater discipline for investment funding allocation, once evaluation practices are adopted to prioritize investment projects by reference to their overall viability (technical, financial, economic, environmental). The program's direct economic benefits will be those ensuing from the investment projects it funds.

2. Risks

4.18 The risks associated with this program have to do with possible delays in implementing institutional reforms because of the new laws that will be required in some instances, and the requisite internal administrative changes. The best way to minimize these risks is to build into the program incentives for municipal governments to adopt major changes – such as the prospect of being able to refinance their debt – as a condition precedent to receiving funding for priority investments. Moreover, the proposed Central Executing Unit, working proactively and in concert with the provinces, will get the necessary processes going and expedite them, and help build consensuses with local communities.

4.19 Adjustments to taxation instruments as called for in the Federal Fiscal Pact may diminish municipalities' own revenues. Countering this eventuality will be the planned tax-administration strengthening projects, which will boost tax yields, and the adoption of revenue-sharing arrangements to offset eventual revenue losses, as also provided in the Federal Fiscal Pact.

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Logical Framework

	INDICATORS	MEANS OF VERIFICATION	ASSU
lf-sustaining municipal	- Municipalities are better equipped to generate and sustain current savings and have greater financial autonomy.	- Central Executing Unit (CEU) monitoring reports - Municipalities' annual budget outturns	- Stable economy - Federal is still c
palities' tax, financial, and ficiency	- By the end of the program, the efficiency and quality of municipal management has improved, as measured by: [1] . a real increase in own resources of at least 10% . an increase in investment proportional to the growth in current saving . total debt stock not exceeding 50% of current revenues . debt service (principal and interest) held to 15% of current revenues . drop in the number of employees needed to keep a maximum ratio of 8 employees per 1000 population	- Municipalities' annual budget outturns - CEU monitoring reports	- Federal is still c
work for municipalities' access to et	- The municipalities secure private finance (10 operations)	- External monitoring report	- Favorab conditio domest internat market

/ These indicators are based on model Reform and Investment Plans for the nine municipalities in the indicative sample used in preparing the program, as well as information on the last three budgetary outturns for 147 municipalities having expressed an interest in joining the program.

	INDICATORS	MEANS OF VERIFICATION	ASSU
S			
in the following areas: l management and tax ration management and government fficiency	The following reform projects have been implemented in accordance with the evaluation benchmarks identified (see table of monitoring benchmarks): - Comprehensive reform of financial management and tax administration (integrated systems for tax administration, accounting and budgeting, expenditure control) and updating of the property roll system - Comprehensive reform of municipal administration (management information systems, human resources management, city planning, delivery of municipal services)	- CEU monitoring reports - External monitoring reports on the program	- Municip governr political to imple reform
ents priority municipal needs for and public infrastructure)	- Bid documents and contracts have been approved for investment projects under way (in municipalities that are meeting their reform targets) which are eligible and are priorities in any of the following sectors: . City and rural roads . Storm drains, flood control structures . Parks and recreation . Solid waste collection and disposal . Street lighting . Transit terminals . Environmental protection and improvement	- CEU monitoring reports - Reports on disbursements approved and processed	- The Bar tenderin procure are adh - Approve and cor timetabl adhered
al private borrowing s the structuring of mechanisms to municipal sources of long-term	- Arrangement for municipal private borrowing is in place, including the following phases: . Study on market access avenues is completed. . 10 pilot projects for municipal securities offering have been launched. . Municipal financial reporting model has been devised. . At least three information seminars on the capital market have been held.	- Consultants' and CEU reports - External monitoring reports on the program	- Conditic private c and inte market a

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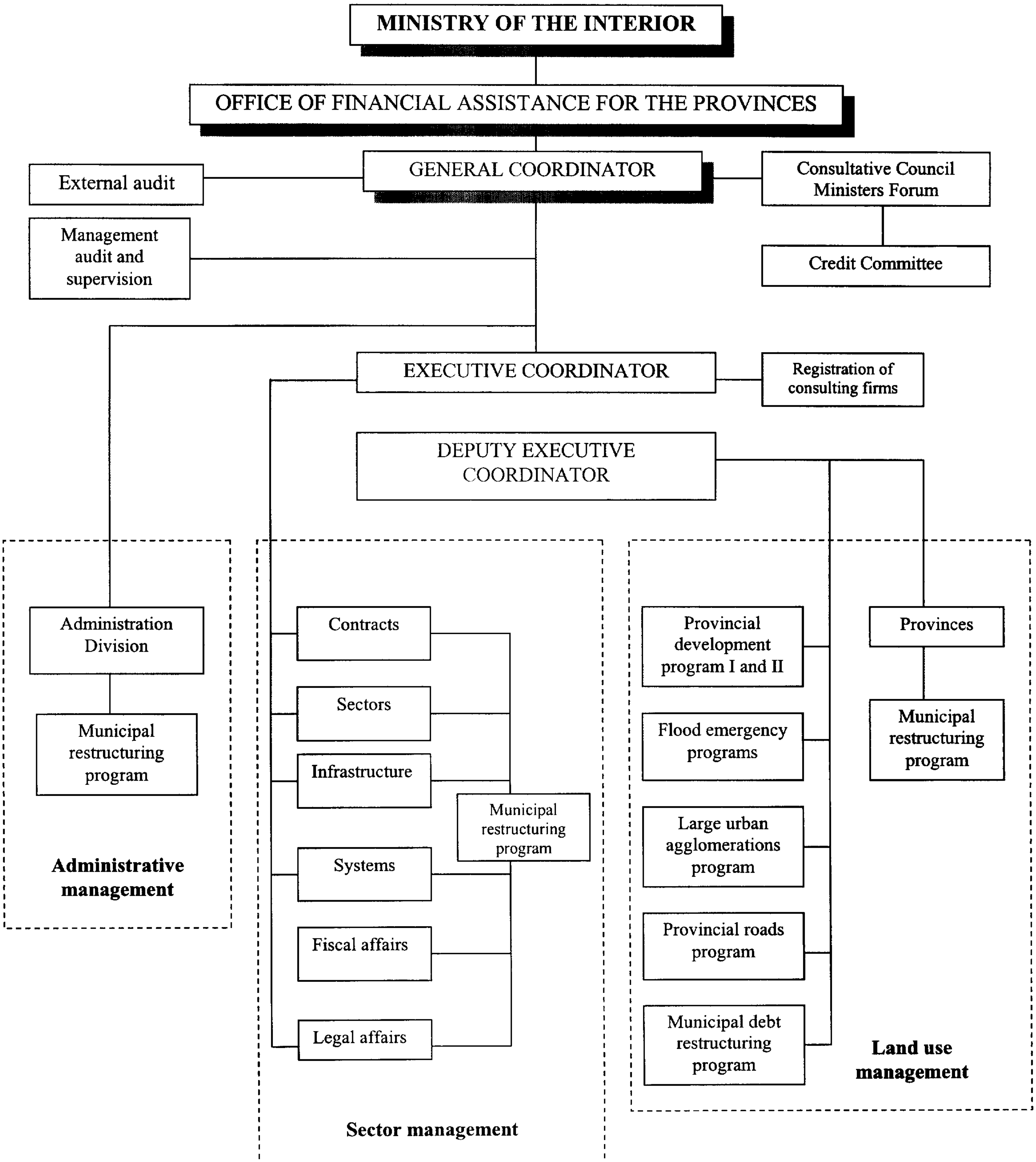
MONITORING BENCHMARKS [2]

Indicator	Number of municipalities			
	Year 1	Year 2	Year 3	Year 4
odes and municipal ordinances updated and operational	95	80	95	30
ll, tax collection, and compliance monitoring systems in place	95	80	95	30
ated financial management systems (budgeting, accounting, cash gement, procurement, human resources)	45	75	90	90
ipal property rolls updated	95	80	95	30
gement information systems in place	45	75	90	90
mer service systems instituted	95	80	95	30
izational structures reviewed and improved	45	75	90	90
ating processes completed			5	5

2/ These benchmarks are based on model PRIs for the nine municipalities in the indicative sample used in preparing the program.

MUNICIPAL REFORM AND DEVELOPMENT PROGRAM

ORGANIZATION CHART



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PROCUREMENT PROCEDURE AND TIMETABLE
(thousands of U.S. dollars)

	Year 1		Year 2		Year 3		Year 4		Tota
	ICB	LCB	ICB	LCB	ICB	LCB	ICB	LCB	
FORM PROJECTS									
Consulting services									
No. of contracts	135	195	124	131	137	192	42	106	1,06
Average contract value	210	100	200	100	200	100	200	100	
L CONSULTING SERVICES	**28,350**	**19,500**	**24,800**	**13,100**	**27,400**	**19,200**	**8,400**	**10,600**	**151,35**
Equipment									
No. of contracts		330		255		290		140	1,01
Average contract value		30		30		30		30	
L EQUIPMENT	**0**	**9,900**	**0**	**7,650**	**0**	**8,700**	**0**	**4,200**	**30,45**
Construction and furnishings									
No. of contracts		70		80		80		20	25
Average contract value		60		60		90		100	
L CONSTRUCTION AND ISHINGS	**0**	**4,200**	**0**	**4,800**	**0**	**7,200**	**0**	**2,000**	**18,20**
L REFORM PROJECTS	**28,350**	**33,600**	**24,800**	**25,550**	**27,400**	**35,100**	**8,400**	**16,800**	**200,00**
INVESTMENT PROJECTS									
No. of contracts		50		80		101		70	30
Average contract value		800		1,000		1,000		800	
L CONTRACTS	**0**	**40,000**	**0**	**80,000**	**0**	**101,000**	**0**	**56,000**	**227,00**
L INVESTMENTS	**28,350**	**73,600**	**24,800**	**105,550**	**27,400**	**136,100**	**8,400**	**72,800**	**477,00**
IAL CONTRACT TOTAL		**101,950**		**130,350**		**163,500**		**81,200**	**477,**
al percentage		**21.37%**		**27.33%**		**34.28%**		**17.02%**	**1**

nternational competitive bidding
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LEG/RG1/AR-0711
Original:Español

PROPOSED RESOLUTION

ARGENTINA. LOAN /OC-AR TO THE ARGENTINE NATION
(Program for the Reform and Development of Argentine Municipalities)

The Board of Executive Directors

RESOLVES:

That the President of the Bank, or such representative as he shall designate, is authorized, in the name and on behalf of the Bank, to enter into such contract or contracts as may be necessary with the Argentine Nation, as Borrower, for the purpose of granting it a financing to cooperate in the execution of a reform and development program for its municipalities. Such financing will be for the amount of up to two hundred and fifty million dollars of the United States of America (US$250,000,000), which are part of the Single Currency Facility of the Ordinary Capital resources of the Bank, and will be subject to the "Special Contractual Conditions" and the "Terms and Financial Conditions" of the Executive Summary of the Loan Proposal.