

PROGRAM FOR MUNICIPAL STRENGTHENING AND DEVELOPMENT

(NI-0156)

EXECUTIVE SUMMARY

Borrower:	Republic of Nicaragua	
Executing agency:	Instituto Nicaragüense de Fomento Municipal (INIFOM), with the participation of beneficiary <i>municipios</i> .	
Amount and source:	IDB (FSO foreign exchange):	US\$12,000,000
	Local Counterpart:	<u>US\$ 3,000,000</u>
	Total:	US\$15,000,000
Financial terms and conditions:	Amortization period:	40 years
	Grace period:	10 years
	Disbursement period:	4 years
	Interest rate:	1% for the first 10 years, 2% thereafter
	Inspection and supervision:	1.0%
	Credit fee:	0.5%
Objectives:	The program's general objective is to strengthen the financial and institutional capacities of the municipal governments to enable them to cope with the growing challenges of urbanization and to improve local services and infrastructure.	
	The program's specific objectives are: (i) ensure institutional strengthening of the participating municipal governments to enhance their financial capacity and efficiency in the provision of services; (ii) promote more controlled and environmentally sustainable urban development; and (iii) strengthen INIFOM to enable it to expand technical assistance and training for the municipalities, develop municipal management instruments and methods, and strengthen its capacity to formulate and assess local development proposals.	

The program strategy is to provide incentives to the municipal governments of the secondary cities to adopt sound practices for municipal management. In each of the municipal governments, the program will finance an institutional modernization and reform plan that will include a set of agreed-upon targets for administration, finance, provision of services, environmental management and urban development planning. As the municipal governments reach these targets, they will gain access to the resources earmarked for priority investment projects. At the end of the program, it is expected that there will be a number of municipal governments capable of responding more adequately to the urbanization process and to the demands of citizens for services and infrastructure.

Description:

The program is aimed at 16 municipal governments of secondary cities facing the challenges of urbanization. To respond to the outlined objectives, the program has been divided into three components:

Component 1. Municipal Strengthening and Development (US\$5 million). This component will finance the preparation, implementation and monitoring of the Municipal Action Plans (MAPs) for participating municipios. The MAPs will identify, on a case-by-case basis, the institutional strengthening activities required by the municipio in the following areas: (i) municipal administration and finance; (ii) service management; (iii) increasing environmental and natural resource management capacity; and (iv) implementation of urban planning and development practices.

Component 2. Municipal Investments (US\$7 million). The funds earmarked for investment projects will be used as an incentive for achieving the targets contained in the MAPs with respect to the adoption of measures and sound practices for municipal management. The investment projects that may be financed under the program include: (i) urban transportation infrastructure; (ii) infrastructure for the disposal and treatment of solid waste; (iii) systems for storm drainage and catchment of rainwater in reservoirs; (iv) green areas, forest areas, or high-value environmental areas which serve to mitigate the municipio's vulnerability to natural disasters or help make better use of natural resources; and (v) protection against erosion and flooding. In the case of investments in markets, terminals, slaughterhouses, cemeteries, restoration of historical heritage, and the disposal and treatment of solid waste, the program will study the possibility of private sector involvement. The eligible projects in this program will complement those funded through the FISE, since FISE makes investments in rural and periurban areas with high poverty rates, while this new operation will finance investments in municipal services and infrastructure in secondary cities. Coordination of the investments funded by the FISE and INIFOM is based on the

Municipal Development and Investment Plans, which are the result of the Municipal Planning System developed jointly by INIFOM and the FISE.

Component 3. Strengthening of INIFOM (US\$2.56 million). This component will finance activities to support INIFOM so that it can take charge of coordinating, developing and supervising the coverage and quality of municipal training and technical assistance (T&TA) services. At the same time, it will finance the development of municipal management instruments and activities to enable INIFOM to expand its capacity to assess and prepare municipal development policy proposals. The technical assistance for INIFOM will help strengthen interagency ties between the FISE and other government agencies that work at the local level.

**Program's
strategic
framework:**

The program's proposed strategic framework is the Enhanced Strategy for Economic Growth and Poverty Reduction (ERCERP), which emphasizes the municipio's role in providing better services and infrastructure for the local population. The Bank's strategy is to support the efforts of the Government of Nicaragua to reduce poverty in the context of implementation of the ERCERP. The program is consistent with the ERCERP because it seeks to strengthen the capacity of municipal governments to ensure interagency cooperation at the local level, increase their capacity for project execution, encourage citizen participation and promote local development.

The operation is also consistent with the Bank's Subnational Development Strategy (SDS), highlighting the importance of assisting the central government to provide better training and technical assistance to the *municipios*; establish systems of municipal financial administration to increase transparency and governability; help strengthen the overall institutional capacities of the *municipios*; and lay the groundwork for sustained improvement of municipal finances.

**Environmental
and social
review:**

The program's strategy consists of supporting better planning for the best use of the land and the strengthening of environmental and natural resource management by the *municipios*, and incorporating environmental concerns into the municipal project cycle.

The program also establishes that, in order to make the investments, the municipality must attain a set of targets for institutional modernization, one of which is the adoption of the Environmental Management System developed by the FISE with the help of the Bank.

The program will have a positive social impact by introducing participatory municipal planning methods, leading to urban development programs to control unregulated settlements, and facilitate the planning and provision of local services and infrastructure. It will thus help improve the living conditions of the *municipio's* inhabitants in general, and in particular, those living in areas of urban expansion.

Benefits:

The participating municipal governments will benefit from the program, since it will provide them with technical assistance to expand their capacity to generate more income and modernize the management of municipal services. In addition, they will have greater technical and financial means to confront the challenges of urban growth and respond more efficiently to the demand for local services and infrastructure. Upon program completion, the *municipios* will have strengthened their institutional and financial capacity, and, thus, will be in a better position to promote local development and help deepen decentralization in Nicaragua.

With the strategies for municipal government modernization, this program will facilitate the introduction in Nicaragua of a model under which access to investment funds is subject to the adoption of reforms and sound practices in municipal management. The adoption of sound practices will be possible because the program will finance the implementation of a comprehensive method for training and technical assistance for municipal management, which has been successfully implemented in other *municipios*, such as San Pedro Sula, Honduras. The program is based on the approach that sustainable improvement of local institutional performance is only possible if the reforms and sound practices encompass all different areas of municipal management.

Risks:

At both the national and municipal levels, there is at the same time high turnover of personnel when the political administration changes. This is a risk to the program to the extent that the professionals and technicians trained in the next few years may be replaced by future administrations. The program seeks to mitigate this risk by increasing the technical value of the municipal employees, thereby making it more costly for the municipality to replace them. This increase in value will be possible with the professional training and technical assistance included in this program, and with the emphasis given to the adoption of municipal management systems that require skilled staff to operate them.

The risk to the program, caused by the possible replacement of INIFOM officials after the upcoming national elections, has been addressed in two ways: (i) the program has been developed in consultation with municipal authorities that will press for program continuity; and (ii) the board of directors of INIFOM will only have partial turnover because the municipal representative on the board, who fully understands the program's purpose, will remain the same.

The current weak coordination in the area of municipal training and technical assistance might be a risk if INIFOM does not coordinate the supply of technical assistance with the participating *municipios*. To reduce this risk, the following measures have been taken: (i) a logical framework workshop has been conducted in which the agencies that are funding projects with INIFOM have explained their programs and discussed ways to achieve greater coordination; (ii) funds have been included for the design of a national technical assistance and training program, which will serve to increase assistance to municipalities, regardless of the provider; and (iii) the program will be managed in the *municipios* by a modernization committee that will have, among its duties, that of coordinating all municipal institutional strengthening activities implemented, regardless of the source of financing.

**Special
contractual
clauses:**

Conditions precedent to the first disbursement will be: the agreement for the transfer of funds must be signed by the borrower and INIFOM (paragraph 3.1).

The Operating Regulations prepared as agreed upon by the Bank and approved by INIFOM must be submitted (paragraph 3.14).

A management and accounting contract system must be set up in INIFOM that will be adequate to manage the program's resources (paragraph 3.2).

**Social sector
classification
and poverty
reduction:**

The proposed program will strengthen the capacity of the municipal governments to respond to the demands of citizens, but does not contemplate any activities or mechanisms focusing on investments to directly alleviate poverty. Based on the available information, the operation qualifies as a social equity enhancing project, as described in the Bank's key objectives, contained in the Report on the Eighth General Increase of Resources.

**Exceptions to
Bank policy:**

None.

Procurement: The procurement of goods and services will be in accordance with Bank policies. International competitive bidding will be required for contracts in excess of US\$1 million for construction works; US\$250,000 for related goods and services and US\$200,000 for consulting services. Works, goods and consulting services not exceeding these amounts will be subject to the procurement procedures stipulated in Nicaraguan legislation, provided that they do not conflict with the Bank's procurement procedures.

I. FRAME OF REFERENCE

A. Urban Development and Demand for Services

- 1.1 The country of Nicaragua is divided into 15 departments, two autonomous regions and 151 municipalities. The total population of the country is approximately five million, of which 56.4% live in urban areas.¹ Managua, with a population of approximately one million, is the major urban and economic center of the country. In addition to Managua, there are 21 cities with populations of 20,000 to 150,000 inhabitants and which together cover about 25% of the total population of Nicaragua.²
- 1.2 Nicaragua is in full urban expansion. In the last decade, the urban population grew at an annual rate of 3.4%, compared with 2.2% for rural population.³ Population growth trends indicate that, in approximately 20 years, the urban population of Nicaragua will double. A principal element in the urbanization process is the flight from rural areas. In fact, for every three persons who abandon their place of birth, two head for the cities. The preferred urban center for immigrants was, for several decades, the city of Managua, but this has been changing in favor of the secondary cities.
- 1.3 In the next few years, the secondary cities will have to face a growing demand for local services and infrastructure. Although the response to this demand is a national issue, the truth is that a large part of the solutions fall on the municipal governments because they are responsible for: (i) the construction or upgrade of the urban transportation infrastructure; (ii) the construction or upgrade of infrastructure for the disposal and treatment of solid wastes; (iii) the upgrade and expansion of the runoff drainage system; (iv) the provision of forested and green areas; (v) the construction of barriers against erosion and floods; and (vi) other municipal infrastructure and services, such as markets, terminals, slaughterhouses, public cemeteries and infrastructure that will foster local economic development. In addition, there is a growing recognition of the importance of municipal governments in defining and implementing national strategies, including such issues as poverty reduction, local development and the battle against HIV-AIDS.
- 1.4 To cope with the increased demand for local services and infrastructure, these municipal governments will have to go through a radical process of institutional modernization, which may include administrative and financial reforms; changes in

¹ Urban population is defined in Nicaragua as the inhabitants of departmental and municipal areas and population concentrations of more than 1,000 inhabitants which have certain features, such as street layout, electricity service and commercial and/or industrial establishments.

² This group of cities is referred to as secondary cities in contrast to Managua, which is the principal city of Nicaragua.

³ Statistical compilation from the *2000 Report on Human Development in Nicaragua*.

the manner in which they provide municipal services and changes and reforms; the management of their natural resources and the environment and in urban development planning methods. The central government will also be required to modernize the method in which training and technical assistance are provided to the *municipios* (strengthening of the Instituto Nicaragüense de Fomento Municipal), and to channel investment funds to support urban development.

B. Municipal governments of the Secondary Cities

- 1.5 There are three factors for determining the municipal governments' ability to respond to the challenges of urbanization: the role that decentralization gives to the municipalities, their financial/administrative capacity, and their ability to manage urban development.

1. Decentralization and the Role of the *Municipios*

- 1.6 Although Nicaragua has made major advances in transferring the duties of service provision and infrastructure to the municipalities, a number of challenges remain to be resolved on the subject of balance between the obligations of expenditure and resources available to the municipality. Indeed, many municipalities, whether due to technical, administrative or financial shortcomings, do not adequately fulfill their responsibilities in matters involving: (i) planning, regulation and oversight of land use and urban, suburban and rural development; (ii) construction and maintenance of streets, sidewalks, railway platforms, parks and plazas; (iii) collection and treatment of solid wastes; (iv) rainwater drainage; (v) operation of markets, slaughterhouses and public cemeteries; (vi) promotion of culture, sports and recreation; (vii) protection of archaeological and historical heritage; (viii) promotion and development of tourism; and (ix) development of transportation and communication methods.
- 1.7 The two major challenges concerning municipal finances are:
- a. **Lack of a proper intergovernmental transfer system.** According to the General Budget of the Nation for the Year 2001, intergovernmental transfers made up only 1% of total tax receipts. Not only is this figure one of the lowest in Central America, but it defines, on an *ad hoc* basis, what makes municipal financing and budget planning difficult. To confront the deficiencies of this system, the Government of Nicaragua, with the support of the World Bank,⁴ has implemented a pilot program for intergovernmental transfers that will result in the presentation and submission of a draft law.

⁴ The World Bank Protierra 2 Program is aimed at expanding the institutional capacity of municipal governments in rural areas and investing in regions of less than 10,000 inhabitants. It also seeks to support the Government of Nicaragua in improving the intergovernmental tax ratio system.

- b. ***Municipal tax deficiencies.*** The Law of Municipalities (Law No. 40, amended by Law No. 261) and the Law of Tax Justice (Law 257) provide that the municipalities are responsible for the collection of real estate taxes (RET), commercial registrations, sales tax (ST), taxes on municipal services, fees for improvements, and other minor sources of revenue such as permits and fines. The National Assembly is responsible for determination of tax aliquots and approval of municipal tax rate programs, while the municipal governments handle tax administration. Due to deficiencies in municipal tax administration and the absence of technical mechanisms for revising tax aliquots, the municipal governments cannot mobilize funds which could potentially be generated locally.

2. Administrative and financial capacity of the municipalities

- 1.8 To fulfill their duties, the municipal governments of the secondary cities have a per capita revenue of approximately US\$17.⁵ Such revenue is derived from the collection of taxes (52%); fees and permits (16%); central government transfers (5%); grants (14%); financial revenue (2%); and other minor sources of revenue (12%).⁶ Of the US\$17 in per capital revenue, approximately US\$3.5 are earmarked for expansion of infrastructure and local services, while the rest (US\$13.5) goes to pay current expenditures, especially wages and salaries. Investments are financed almost exclusively with grants and transfers, which shows that the local tax efforts have little impact on the expansion of municipal services and infrastructure.
- 1.9 The municipal governments have current expenditures that are difficult to reduce (about 62% goes toward the payment of salaries and 32% to the procurement of goods). The low staff productivity and inefficient spending impede the generation of current savings, and consequently, reduce the ability to fund investments. The source of the inefficient spending is found in the lack of criteria in the management of municipal services, excessive red-tape with respect to administrative procedures, lack of human resource management methods, and the absence of finance and tax administration systems to help improve efficiency and transparency of municipal operations.⁷
- 1.10 According to a recent study on the impact of implementing cadastral systems, the municipal governments have great potential to mobilize resources, in particular, with respect to real estate taxes. In a sample of 21 municipalities, it was shown that

⁵ These data are from the Year 2000. Municipal revenue of the secondary cities is relatively low when compared with approximately US\$37 per capita generated by Managua.

⁶ These sources include the sale of goods and services, fines, reposessions and repayments.

⁷ Among the secondary cities, only 15% of the municipalities have a procurement system, 30% have a project and investment management system, none have procedures for staff performance evaluation, and only 25% have a financial management system.

the municipalities only collected 30% of the potential value of real estate taxes.⁸ The main reasons for this weak taxing effort is based on the presence of incomplete tax bases and the absence of tax administration systems that would allow greater efficiency in invoicing, collection, inspection and recovery of delinquencies.

3. Municipal capacity with respect to managing urban development

1.11 In general, the shortfalls of municipal urban development management are in the following areas:

- a. **Urban development planning.** Although a municipal responsibility, practically none of the municipal governments of the secondary cities have a master urban development plan which would permit them to: (i) regulate, supervise and enhance the use of land; (ii) direct urban growth; and (iii) better coordinate investments in terms of current and future requirements of municipal infrastructure and services. As a result of this shortfall, municipal investments do not correspond to a strategic vision of urban development, are made without consideration to citizen demand, and tend to focus on works that are small and poorly coordinated, to which can be added the municipalities' lack of experience in the preparation and evaluation of investment programs that put development plans into effect.
- b. **Environmental and Natural Resource Management.** Generally, the municipalities do not have an institutional agency that will enable them to fulfill their duties of environmental and natural resource management. The absence of a specialized institution with environmental technical capacity indicates the minor importance which has been given to issues such as environmental licensing of investment projects, the development of environmental education campaigns and the preparation of municipal environmental management programs and response to natural disasters.
- c. **Municipal services management.** The most critical problems in service management are: (i) absence of cost accounting systems to facilitate independent financial management of services; (ii) presence of rate systems that have been defined without considering the need to cover operating costs and future investments to expand service coverage; (iii) lack of regulations to promote private sector participation; and (iv) absence of quality and operating rules to guarantee the interests of the citizens. In addition to these problems, several municipalities have directed resources to activities that, by their nature, should have been shifted to the private sector.

⁸ Report on the Impact of the SISCAT on real estate tax collection. DANIDA Project NIC-98-015. Municipal Cadastral System. Phase III.

C. Technical Assistance to the Municipalities

1. Instituto Nicaragüense de Fomento Municipal (INIFOM)

- 1.12 The Instituto Nicaragüense de Fomento Municipal (INIFOM) is an autonomous entity of the central government charged with facilitating access to technical assistance and training by the municipalities while promoting local development. It was created by Decree No. 497 in 1990 and changed its status by means of Law No. 347 of 27 June 2000 (known as the Basic Law on INIFOM) and by Decree No. 75-2000 containing the respective regulations. The new legal framework expands INIFOM's responsibilities so that, in addition to strengthening the municipalities, this agency promotes the municipalities' development capacities as a means to reduce poverty. INIFOM's new responsibilities are consistent with the Estrategia Reforzada de Crecimiento Económico y Reducción de la Pobreza (ERCERP), which assigns to INIFOM the key function of strengthening local capacity and creating the conditions for deepening decentralization.
- 1.13 The Board of Directors of INIFOM is characterized by maintaining a balance between the representatives of the central government (Ministry of Education, Ministry of Transportation and the FISE) and the municipalities (two Mayors and a representative of the Nicaraguan Association of Municipalities). The 2001 budget for INIFOM is US\$22 million, of which US\$650,000 is earmarked for operating expenses (INIFOM has 170 employees); US\$1.25 million are transfers from the central government to support the poorest municipalities; US\$16.1 million are funds for the municipal strengthening and development programs and projects carried out by INIFOM (50% are financed by a loan from the World Bank; 12.5% are other loans; and 37.5% comes from outside grants); the remaining US\$4 million are funded by the Tesoro General de la Nación (National General Treasury) to cover local contributions.
- 1.14 Since its creation, INIFOM has carried out an important function as the executing unit of various municipal strengthening programs which, in general, have been characterized by a non-integrated approach. The experience that INIFOM has accumulated over the last 10 years has not yet been tapped to design a sustainable national technical assistance and training program (T&TA) covering the range of institutional challenges facing the municipal governments. Institutional studies conclude that the cause of this shortcoming has been that the project executing units within INIFOM have not helped to consolidate this institution, a situation that is changing gradually.

2. Other public institutions providing T&TA to municipalities

- 1.15 In addition to INIFOM, the major public institution providing T&TA to the municipalities is the Fondo de Inversión Social de Emergencia (FISE) (Emergency Social Investment Fund). The FISE has begun to delegate the management of its

project cycle to the municipal governments. The Bank's current project with the FISE has the financial resources to support the introduction of municipal participatory microplanning and the delivery of technical assistance to strengthen the municipal governments' capacity to design, execute and maintain social infrastructure works. The municipal strengthening efforts supported by the FISE are aimed at the poorest municipalities and rural areas, and therefore have not covered the secondary cities. This operation is designed to achieve complementarity between the FISE and INIFOM, since it will cover the demand for T&TA by a group of municipalities not served until now, while developing the instruments of municipal management (particularly the tax and finance management systems) which are necessary to give sustainability to the participatory planning and delegation of investment responsibilities in the *municipios* supported by the FISE.

- 1.16 The major tasks to be carried out in the next few years to improve municipal T&TA services are: (i) strengthen the knowledge of municipal demand for institutional strengthening; (ii) expand supply by developing municipal management methods and instruments; (iii) establish a system for accreditation of suppliers of such services; and (iv) establish a national framework for better coordination and cooperation between supply and demand for T&TA services. To do so, INIFOM will have to guarantee that it is able to take on the role as the national agency responsible for regulating, executing and coordinating municipal strengthening efforts.

D. The Program's Strategic Framework

- 1.17 The program's proposed strategic framework is the Estrategia Reforzada de Crecimiento Económico y Reducción de la Pobreza (ERCERP), which emphasizes the municipality's role in providing better services and infrastructure to the local low income population. The Bank's strategy is to support government efforts, within the framework of the ERCERP, to reduce poverty. The program is consistent with the ERCERP because it seeks to strengthen the capacity of municipal governments to assume the role of leader and participant in local interinstitutional coordination.
- 1.18 The operation is also consistent with the Bank's Strategy for Subnational Development (EDS), which emphasizes the importance of assisting the central government in offering improved T&TA services to the municipalities, establishing municipal financial management systems to enhance local governability and transparency, integral strengthening of municipal institutional capacity, and laying the groundwork for sustained growth of local financing.
- 1.19 The program has taken into account the operations financed by the Bank in the area of local development. In particular, the proposed program, with its approach to municipal strengthening, will complement the activities of the Program for Local Development of the Atlantic Coast (NI-0107) aimed at the strengthening of

autonomous regional governments. The technical assistance package in this program supplements the FISE's efforts to encourage participatory microplanning and decentralization of project cycle management by the municipal governments.

- 1.20 The operation has been designed in consultation with other donors who support INIFOM's municipal development programs and with representatives of various municipal governments. The technical concept and content were discussed and agreed to at a program planning workshop attended by Asdi, the World Bank, GTZ and the Danish International Development Agency (DANIDA), which discussed the program's participatory methods, and how the program will complement the institutional strengthening efforts being carried out through INIFOM. In addition, a workshop was held with several representatives of the municipal governments that will participate in the program, for the purpose of defining the program approach and components. At the workshop, it was clear that the municipalities assign high priority to the program

II. THE PROGRAM

A. Objectives

- 2.1 The program's general objective is to strengthen the financial and institutional capacity of the municipal governments to enable them to cope with the growing challenges of urbanization and to improve local services and infrastructure.
- 2.2 The program's specific objectives are: (i) institutional strengthening of the participating municipal governments to increase their financial capacity and provide more effective services; (ii) promote more controlled and environmentally sustainable urban development; and (iii) strengthen INIFOM to enable it to expand technical assistance and training to the municipalities, develop municipal management instruments and systems, and strengthen its capacity to formulate and assess local development proposals.

B. Program Scope

- 2.3 This program will help INIFOM acquire the capacity to integrally strengthen the municipalities and have a set of municipal management systems and instruments that can be used nationally. The program seeks to promote the implementation of institutional reforms and sound practices of municipal management, by granting resources for municipal investment, whose access is subject to the municipality's attainment of a set of institutional development targets.
- 2.4 To the extent that this program achieves its objectives, the participating municipal governments will have a multi-annual investment program which could form the basis for future local activities. Furthermore, if the participating municipal governments succeed in strengthening their finances, administration and management, they will be in a better position to be counterparts in various national programs implemented on the local level, including programs currently funded by the FISE.
- 2.5 To pave the way for modernization of the municipal governments, the program will support INIFOM in strengthening its role as the national institution responsible for coordinating, developing and supervising the T&TA services. The strategy for modernizing and giving sustainability to the T&TA services is for INIFOM to become a supply and demand coordinator, so that the technical assistance and training will be rendered by consulting firms, independent consultants, NGOs, technical training institutes and academic centers. Enhanced T&TA is an essential element for municipal governments to become active in local development and decentralization.

C. Criteria for Selection of Participating Municipalities

- 2.6 The municipalities will be selected on the basis of the following criteria: (i) population; (ii) unmet demand for technical assistance; and (iii) regional balance. In applying these criteria, municipalities have been selected with an urban base exceeding 20,000 inhabitants; who do not receive assistance under any other municipal strengthening and development programs in the same areas of intervention as those covered by the program; and are distributed throughout the various geographic regions of the territory of Nicaragua. The municipalities that have fulfilled these criteria and will be invited to participate in the program are: Estlí, Ocotal, Jalapa, Tipitapa, Ciudad Sandino, San R. del Sur, Granada, Rivas, Jinotepe, Diriamba, Boaco, Masaya, Matagalpa, Jinotega, Bluefields, and Pto. Cabezas. Three of these municipalities (Granada, Rivas and Masaya) already have the necessary studies to begin the program, while the rest have verified the existence of sufficient demand. The total urban population of these *municipios* is 780,000 inhabitants.
- 2.7 The selected *municipios* will have to fulfill the conditions of eligibility in order to participate in the program. These conditions include: (i) presentation of a letter of commitment with the backing of the Municipal Council in which the municipality undertakes to contribute 20% of the total investments under the program; and (ii) presentation of a financial and institutional assessment prepared according to the program's methodologies supplied by INIFOM, and which include a preliminary action plan. In the case of the municipalities of Bluefields and Puerto Cabezas, or in other justified situations, INIFOM will assist the municipalities to fulfill the second condition.

D. Program Components

- 2.8 To meet these objectives, the program has been divided into three components: (i) municipal strengthening and development; (ii) municipal investments; and (iii) strengthening of INIFOM.

1. Component 1. Municipal Strengthening and Development (US\$5 million)

- 2.9 This component will finance the preparation, implementation and monitoring of Municipal Action Plans (MAPs), whose average cost is estimated to be US\$300,000. The methodology and content of these plans have been designed with the active involvement of the authorities and technicians of a sample of municipalities (Masaya, Rivas and Granada), which has led to verification of demand and appropriation under the MAPs. The activities of institutional reform to be included in the MAPs will be defined on a case-by-case basis, according to the municipality's needs and its ability to execute such reforms. The MAPs will include: (i) modernization of finances and management; (ii) strengthening of municipal services; (iii) implementation of local environmental and natural resource

management; and (iv) introduction of urban development planning. The list of activities that may be included in the MAPs is as follows:

- 2.10 **Finance and Administration Modernization.** This includes: (i) assessment and execution of a finance strengthening plan; (ii) reengineering of finance and tax management procedures; (iii) implementation of an integrated municipal finance management system; (iv) implementation of a tax management system;⁹ (v) the mapping of data to expand and upgrade the municipal cadastral database;¹⁰ (vi) implementation of rules and procedures for procurement of goods and contracting of services and works; (vii) introduction of a human resources management system, and (viii) design and implementation of a local training program. This program will include the educating of municipal officials to include, among other things, the participation of women and other excluded groups (including ethnic groups) in the municipality's development.
- 2.11 **Strengthening of Municipal Services.** Technical assistance will be financed for: (i) preparation of assessments and plans for modernization of municipal services; (ii) outsourcing, corporatization or privatization of services with greater potential for the private sector to provide them; (iii) conversion of a portion of municipal services into independent cost management centers; (iv) review and upgrade of tax and fee administration procedures; (v) adoption of municipal ordinances for regulating quality and operation of municipal services; and (vi) creation of municipal consortiums for the provision of municipal services. If, as a result of these improvements, revenue is increased through the collection of taxes, this revenue will be used to expand the coverage and improve the quality of service.
- 2.12 **Strengthening of environmental and natural resource management capacity.** This area includes training and technical assistance for: (i) formation of an environmental and natural resource management unit within the participating *municipios*; (ii) implementation and upgrade of the FISE environmental management system (guidelines, manuals and procedures of environmental licensing) in the municipal project cycle; (iii) design and implementation of environmental education campaigns to prevent pollution and direct the recycling of solid and liquid wastes; and (iv) distribution of instruments for the preparation of municipal response plans in the event of natural disasters.
- 2.13 **Implementation of Urban Development Planning Practices.** This MAP activity is embodied in the National System of Municipal Planning, adopted by INIFOM

⁹ For reasons of economies of scale and compatibility, the systems will be designed and developed by INIFOM.

¹⁰ The IDB program will further promote cadastral systems, since it will finance the updating of the cadastral database. The adoption by the *municipios* of geographic information systems is part of the Cadastral Modernization Program (SISCAT) financed by the Danish cooperation agency (DANIDA) and the United Nations Development Programme (UNDP).

and the FISE, which includes citizen participation in defining local priorities. It includes: (i) the preparation or updating of an Master Urban Development Plan covering, among other things, land use planning and basic municipal infrastructure; (ii) preparation of a multiannual investment program based on citizen participation; (iii) preinvestment studies for municipal projects to be financed by the program; and (iv) T&TA to strengthen the capacity of the municipal planning technical unit or office to enforce development and urban land use guidelines, and to manage the project cycle.¹¹

2. Component 2. Municipal Investments (US\$7 million)

2.14 Component 2 has been designed to foster attainment of the goals of institutional reform and modernization included in the MAPs. Targets have been specified in each MAP activity to measure the outcomes of institutional modernization efforts. As a result of the MAP initial activities, it is expected that the participating municipality will be able to attain the first four targets of institutional modernization, which in turn will help it access up to 50% of the ceiling of allocable investment funds. These targets are as follows:¹²

- a. *Modernization of municipal management and finances.* Completion of the cadastral registry of urban real estate in the participating *municipio*.
- b. *Improve management of municipal services.* Establishment of two municipal services with independent cost recovery centers.
- c. *Strengthen capacity for environmental and natural resource management.* Submission of an environmental management program for the *municipio*, approved by the Municipal Council, which includes the designation and funding, out of the municipal budget, of an officer to be specifically responsible for implementation and finance.
- d. *Urban development planning practices.* Submission of the final UNDP report, prepared in accordance with INIFOM-FISE municipal planning system, previously adopted by the Municipal Council.

¹¹ This activity will be coordinated with the FISE, which will also promote efforts to strengthen project cycle management capacity in poorer *municipios*.

¹² These targets were established taking into account the assessments of Granada, Masaya and Rivas, together with the data provided by INIFOM based on the cadastral system, municipal information system and financial information system. The methods for verifying attainment of these targets are described in the program's logical framework matrix.

- 2.15 To access the remaining investment funds, the *municipio* will have to attain four more targets defined to measure the depth of reforms in the four areas of MAP activity. These targets are:
- a. *Modernization of municipal management and finance.* 15% increase in real estate tax (RET) receipts for the MAP's first year and generate current savings equivalent to the real estate tax revenues recorded for the last implemented budget.
 - b. *Improving municipal service management.* Recovery of operating and maintenance costs for two municipal services.
 - c. *Strengthening capacity for environmental and natural resource management.* Preparation and approval of municipal projects in compliance with environmental management system launched by the FISE.
 - d. *Implementation of urban development planning practices.* The municipality has identified the urban municipal investments for two years within the UNDP framework, which will first have to be approved by the Municipal Council.
- 2.16 The allocation of investment funds among the participating *municipios* will take into account the size of the urban population and the incidence of poverty according to the latest current official poverty chart. The projects to be funded under the program should have preinvestment studies demonstrating technical, financial, socioeconomic and environmental feasibility. In addition, each of the projects must comply with the following: (i) identify the duties of the local project representatives; (ii) observe the technical rules and national policy guidelines established by the applicable authority; and (iii) include an operating and maintenance program. The minimum investment to be financed under the program will be US\$50,000.
- 2.17 The investments to be financed by the program are aimed at improving municipal services and infrastructure in the secondary cities, and to that effect, they supplement the investments made through the FISE, which emphasize the provision of social infrastructure for the poverty-stricken populations of the rural and periurban areas. The investments financed by the FISE and INIFOM are coordinated in accordance with the Municipal Investment and Development Plans, under the Municipal Planning System, developed jointly by INIFOM and the FISE.
- 2.18 The projects to be financed by the program include: (i) urban transportation infrastructure for the use of motorized vehicles and pedestrians; (ii) infrastructure for the treatment and disposal of garbage; (iii) upgrade and expansion of a runoff drainage system; (iv) investments in green areas, forests or high-value areas to help lessen the *municipio's* vulnerability to natural disasters and to make more effective use of natural resources; and (v) barriers against erosion and floods. In the case of

projects involving markets, transportation terminals, slaughterhouses, public cemeteries, restoration of historical heritage, and treatment and disposal of sewage, the preinvestment studies should contain an analysis of the different financing options, so that the program will finance projects with a high socioeconomic benefit and of no interest to private investors.

- 2.19 When investments are made in services subject to tax collection or other types of payments, the municipal government should ensure that it is taking measures to recover the costs, and that the revenue generated will be used to expand service coverage and improve service quality. Moreover, these investments may be made only if the municipal government has included activities in its MAP for modernization of service management.

3. Component 3. Institutional Development of INIFOM (US\$2,562,000)

- 2.20 This component will assist INIFOM in enhancing its operations as the agency responsible for coordinating, developing and supervising the municipal T&TA services. The component will also finance activities to enable INIFOM to strengthen its capacity to prepare and assess proposals for decentralization and municipal development policies. Specifically, it will finance the activities described below.
- 2.21 **Expansion of Municipal T&TA Services (US\$512,000).** This includes: (i) study of training and technical assistance needs of the various kinds of *municipios*; (ii) valuation and eventual adoption by INIFOM of municipal management instruments developed within the framework of various technical assistance programs that INIFOM has implemented or will implement; (iii) design of a national T&TA program for the *municipios*; (iv) expansion of the training component of INIFOM website; and (v) establishment of indicators for measuring municipal government performance. The program will also finance the establishment of a system for T&TA provider accreditation, which will contain a list of consulting firms, NGOs, educational centers, and individual consultants authorized and certified by INIFOM to provide services to the *municipios*. The establishment of the accreditation system is the central element in the modernization of municipal T&TA services, since only with the providers' improved capacities can these services be given greater sustainability. The T&TA activities called for in the MAPs will be carried out by INIFOM-accredited providers. Therefore, parties interested in providing municipal T&TA services have an incentive to be registered with INIFOM.
- 2.22 **Development of finance and tax management systems (US\$1 million).** This includes the development of finance and tax management systems to be implemented by the participating *municipios* within the MAP framework. These systems will include the drafting of rules and regulations, design of an

implementing strategy, software development and specifications of necessary equipment to be installed for the municipalities.

- 2.23 **Institutional Development of INIFOM (US\$600,000).** This includes technical assistance for the following: (i) upgrading the internal structure of the institution in program-related areas; (ii) reengineering of INIFOM's regional agencies and training of their technical staff; (iii) increasing interinstitutional cooperation with respect to municipal T&TA; and (iv) preparing studies, proposals for municipal development and decentralization policies and laws. With respect to the latter, the program will finance, among other things: the preparation of a model ordinance to regulate the procurement of goods, and the contracting of services and works with the *municipio's* own resources, studies for the development of the municipal finance system, and the preparation of proposals to enhance the legal framework of municipal services, including procedures for third-party provision of such services. INIFOM will also help local governments participate in cooperation networks on subjects such as the ERCERP and the national program against HIV-AIDS.
- 2.24 **Program management, support and supervision (US\$450,000).** The program's management costs include technical assistance to INIFOM units in charge of program activities. The support for program execution and monitoring includes, among other things, the financing of: (i) the promotion and publicizing of the program among the preselected *municipios*; (ii) the contracting of consulting services for the mid-term evaluation and monitoring of the program's outcomes (based on the logical framework indicators); (iii) independent audit of the program; and (iv) annual meetings so that the participating *municipios* can share their municipal management experiences.

E. Scope, Costs and Financing

- 2.25 To gauge the scope of Components 1 and 3, the following have been taken into account: the average cost of three Municipal Action Plans as a consultant's report on the municipal finance management systems, and a study on capacity strengthening activities required by INIFOM. The scope of Component 2 has been measured by taking into account: the *municipios'* current capacity to manage investments, and their ability to meet the local counterpart contribution required by the program.
- 2.26 The cost of the program has been estimated at US\$15,000,000. The IDB funding, equivalent to US\$12,000,000, will come from the Fund for Special Operations (FSO) and will cover up to 80% of the program's total cost. The local counterpart funds, equivalent to US\$3,000,000, will come from the central government. The municipal governments participating in the program must contribute 20% of the investments financed under the program. Contributions from the municipal governments will be used to cover a portion of the local counterpart funds under the program, which may be in cash, materials or staffing.

Table III-1				
Investment Categories (in thousands of US\$)				
	IDB	Local	Total	%
1. Municipal Strengthening and Development	4,000	1,000	5,000	33.3%
2. Municipal Investments	5,600	1,400	7,000	46.7%
3. Strengthening of INIFOM capacity	2,016	546	2,562	17.1%
3.1. Upgrade of municipal T&TA services	411	101	512	
3.2. Development of finance management systems	800	200	1,000	
3.3. INIFOM institutional development	400	200	600	
3.4. Administrative support for execution and supervision	405	45	450	
Subtotal	11,616	2,946	14,562	97.1%
Financing costs	384	54	438	2.9%
1. Inspection and supervision	120		120	
2. Credit fee		54	54	
3. Interest	264		264	
Total Program	12,000	3,000	15,000	100.0%
Percentage	80%	20%	100%	

2.27 The time frame and terms of the proposed operation are as follows:

Source of financing	FSO
Currency:	US\$
Terms:	
Amortization period:	40 years
Grace period:	10 years
Commitment period:	3.5 years
Disbursement period:	4 years
Interest rate:	1% for first 10 years 2% in subsequent years
Supervision:	1%
Credit fee:	0.5% annually on undisbursed balances

III. PROGRAM EXECUTION

A. Borrower and Executing Agency

- 3.1 The borrower will be the Government of Nicaragua. The Instituto Nicaragüense de Fomento Municipal (INIFOM) will be the executing agency. **Evidence that an agreement for the transfer of program resources and program execution has been entered into by the borrower and executing agency must be submitted as a condition precedent to the first disbursement.**

B. Program's Institutional Framework

1. Instituto Nicaragüense de Fomento Municipal (INIFOM)

- 3.2 INIFOM will be accountable to the Bank for the program's execution and coordination. INIFOM's program-related duties are: (i) sign the Fund Transfer Agreement with the Ministry of the Treasury, framework agreements with the municipal governments, and other legal and contractual documents required for the proper implementation of the program; (ii) comply with and ensure that the municipal governments comply with the framework agreements and Operating Regulations; (iii) supervise the attainment of program objectives; (iv) effectively manage resources; (v) prepare and deliver to the IDB the reports set forth in the loan contract; (vi) keep the program's accounting and records of fund use up to date; and (vii) coordinate with the FISE, public and private institutions and agencies for international cooperation, the measures necessary to implement the program. **The submission of evidence that INIFOM has an adequate accounting system and contract administration system to manage the program's resources will be a condition precedent to the first disbursement. This method will guarantee the transparent handling of the program funds.**
- 3.3 INIFOM has designated the Department of Operations as the unit responsible for supervising the MAPs and municipal investments (Components 1 and 2), as well as Component 3. The duties of the Department of Operations include: (i) conducting promotional events and publicity to inform the *municipios*, NGOs, enterprises and others on the program's general rules and regulations; (ii) advise the *municipios* of the program activities, according to the rules established in the framework agreements and Operating Regulations; (iii) assist the municipal governments in preparing the terms of reference and model bidding terms and conditions pursuant to which the municipal government contracts for consulting services for the preparation and implementation of the MAPs; (iv) formulate and apply the terms of reference, and bidding terms and conditions for the contracting of consulting services within INIFOM institutional development component; (v) submit semiannual progress reports, pursuant to the terms specified by the IDB; and

(vi) maintain a system of accredited operators and providers of goods and services who can be contracted by the municipalities to provide services and perform works as contemplated in Components 1 and 2. To assist the Department of Operations to fulfill its duty of program execution, resources have been included in the budget for consulting services on specific subjects.

- 3.4 INIFOM will rely on a Technical Committee formed by the directors of the four departments of INIFOM. This committee will be in charge of coordinating the institutional development activities contemplated in Component 3, of which the Department of Operations will keep this committee regularly informed.

2. Municipal governments

- 3.5 The municipal government that fulfills the requirements for participation in the program may receive funds to carry out the institutional modernization activities and investments set forth in Components 1 and 2 of the program, according to the terms of the framework agreement to be signed by INIFOM pursuant to the respective MAP. A model framework agreement has been drawn up as part of the program's preparatory activities.
- 3.6 The day-to-day program monitoring within the *municipio* will be entrusted to a Municipal Executing Unit (MEU) to be set up for that purpose. The MEU will be headed by a full-time municipal officer (Program Coordinator) assisted by short-term advisors on specific matters such as financial management, contracts and outlays, urban development and municipal strengthening. The experts will be paid as provided under the program and will have contracts by product so that the local technicians in each *municipio* will be implementing the MAPs. The duties of management strategy, evaluation of reforms contained in the MAPs, interprogram coordination, and designation of the program coordinator will be entrusted to the Municipal Modernization Committee to be created for purposes of implementing the MAP. This committee will be formed by the local general directors of the MAP's areas of involvement¹³ and will report directly to the Mayor.
- 3.7 The municipal governments are responsible for the following, among other things: (i) the contracting of consulting services, in accordance with the Bank's rules, for the preparation and execution of activities and studies indicated in the MAPs; (ii) oversee and supervise the financial and material aspects of the contracted services; (iii) process requests to INIFOM for disbursements of the program's funds; (iv) contribute the counterpart funds when due; (v) approve interim and final reports by the hired consultants; (vi) monitor MAP performance indicators and report outcomes to INIFOM; (vii) assist the IDB and INIFOM in general program

¹³ The Modernization Committee will be formed by a maximum of four municipal directors (one for each area of involvement). The Operating Regulations provide for measures to prevent discrimination by sex or ethnic origin in the formation of the Modernization Committees.

supervision and support these organizations in their work; and (viii) prepare the terms of reference, technical, legal, rate and quality specifications, conditions for determining indicators and other requirements, to carry on the processes of outsourcing, corporatization or privatization, as necessary.

- 3.8 In addition to the above, the municipal governments will have the following duties with respect to Component 2: (i) conduct the bidding process for procurement of works and goods; (ii) supervise the material and financial aspects of the projects; (iii) proceed to the final acceptance of works and goods in accordance with the signed contracts; and (iv) as appropriate, handle the necessary environmental authorizations, in accordance with current laws.

3. NGOs, consulting firms, private enterprises, and technical/professional training centers

- 3.9 These organizations will be contracted by the municipal governments to render consulting, technical assistance and training services, supply goods and execute municipal investment projects. These organizations must be accredited by INIFOM.

C. Program Regulatory Instruments

- 3.10 The program will be subject to the rules set forth in the following documents: the loan contract signed by the Republic of Nicaragua and the IDB; the fund transfer agreement signed by the borrower and INIFOM, and the Operating Regulations. The relationship between the eligible municipal governments and INIFOM will be established through the framework agreements, which will stipulate the specific terms which the parties must fulfill for the preparation, financing and execution of the MAPs and projects, setting forth the targets to be monitored. In preparing the program, drafts of the Operating Regulations and the framework agreement were prepared and discussed with Nicaraguan authorities.
- 3.11 The fund transfer agreement will include, at least, the following: (i) commitment from the Ministry of the Treasury to transfer the financing resources to INIFOM; and (ii) INIFOM's commitment to execute the program in accordance with the terms of the loan agreement with the Bank.
- 3.12 The framework agreements between INIFOM and the municipal governments will include, at least, the following: (i) INIFOM's commitments, among which are: (aa) transferring the applicable funds to each *municipio*, once it has fulfilled the conditions and requirements for participation in the program; (bb) advise the municipal governments with respect to program execution; (cc) provide the municipalities with a list of accredited providers of goods and services; (dd) develop and transfer to the municipalities the finance and tax management systems; (ee) process requests for disbursement and other requests submitted by the municipalities within the time periods set forth in the Operating Regulations;

(ii) commitments from each of the *municipios*, among which are: (aa) execute their activities in accordance with the framework agreement and Operating Regulations; (bb) utilize the resources transferred to them solely and exclusively for program activities; (cc) submit the required progress and evaluation reports and all other necessary information so that INIFOM and the Bank can monitor the program's progress; (dd) maintain accounting records that can be easily audited in accordance with widely accepted rules; and (ee) submit evidence that the municipal budget has the funds necessary to contribute the local counterpart funds; (iii) the manner in which the funds will be transferred under the revolving fund mechanism not to exceed 5% of the amount of the funds allocated to each municipality; and (iv) the conditions and mechanism for accessing the investment funds.

- 3.13 The framework agreement will establish the amount of resources allocated to the corresponding municipality, for both institutional modernization activities and investment projects. Any change in the allocation of resources as a result of the annual evaluations by INIFOM and the Bank (paragraph 3.22) will be covered in an addendum to the framework agreement, which will establish the new amount to be allocated, the counterpart's obligation and the manner in which such funds will be spent.
- 3.14 The program's Operating Regulations will govern the activities carried out by INIFOM and the participating *municipios*. The Operating Regulations include, among other things, the following: (i) requirements in order for the *municipios* to participate in the program; (ii) activities eligible for financing; (iii) program execution and approval cycle; (iv) model framework agreement to be signed by INIFOM and the participating municipalities; (v) targets permitting the municipal governments to access the investment funds; and (vi) the program's performance indicators. These Operating Regulations may be amended only by a reasoned written request from INIFOM and the Bank's no objection. **The presentation of the Operating Regulations drafted in accordance with the Bank's requirements and approved by INIFOM is a condition precedent to the first disbursement.**

D. MAP Execution and Approval Cycle and Municipal Investments

1. Promotion

- 3.15 INIFOM will publicize the program by calling the 16 preselected *municipios* to participate in the program and by holding a start-up workshop. The call will consist of an invitation letter that will contain, at least: (i) the requirements for participating in the program; (ii) estimate of the amount of resources available to each *municipio* for the institutional modernization activities and for investments; (iii) the time frame for submission of the required documentation; and (iv) the rules that will govern the activities to be financed. Six months after the first call, there will be a

second call to give the municipalities that were not able to comply with the participation requirements the first time a second chance.

- 3.16 The participation requirements include: (i) submission of an assessment of the municipality's institutional and financial situation, prepared in accordance with the program methodologies supplied by INIFOM, which includes an action plan proposal; and (ii) submission of a letter of commitment, backed by the Municipal Council, in which the municipality undertakes to contribute 20% of the total amount of the investments under the program.
- 3.17 The municipal governments interested in participating in the program must indicate their interest in writing within 30 days following the call. After that period, a start-up workshop will be held with all the municipal governments that have responded. The mayors, council members and technicians who will be involved in the program activities will be invited. This workshop is intended to explain the program's scope and conditions to all interested persons so as to facilitate fulfillment of the participation requirements described in paragraph 3.16. The workshop will also serve to introduce and explain the participation model and MAP methodologies.

2. Selection of the *Municipios*

- 3.18 After the start-up workshop has been conducted, the municipal governments will have 60 days to submit the documentation required in paragraph 3.16.
- 3.19 INIFOM's Department of Operations will verify the documentation required in the call and will prepare a list of the municipalities that complied with such requirements, i.e., those that submitted the assessment of the financial and institutional situation and the letter of commitment from the local counterpart approved by the Municipal Council. The Department of Operations will also prepare a list of the *municipios* that failed to submit the required documents within the specified period. Both lists will be presented to the Board of Directors of INIFOM for its information and approval, and will be sent to the Bank for its no objection. The results of the selection of the participating *municipios* will be made public.

3. Signing of Framework Agreement

- 3.20 INIFOM will sign a framework agreement with the *municipios* that have fulfilled the requirements of the call. The framework agreement will govern the relationship between the parties during the program, including institutional modernization and investment activities. The framework agreement must comply with the requirements set forth in paragraph 3.12.
- 3.21 The amount of investment funds available to each participating *municipio* will be defined using a formula based on urban population size and the incidence of poverty in the respective *municipio*. The funds available for institutional

strengthening activities (Component 1) will be defined using a formula based on the municipal budgets. The funds will be transferred by INIFOM to the participating municipality on a non-reimbursable basis.

- 3.22 The amount allocated to each municipality will be maintained for two years from the date of signing of the framework agreement. After that period, the allocation will be revised by INIFOM and the Bank as part of the annual program evaluation, for which the respective municipality's performance and the progress of the material-financial aspects of the program will be taken into account. The resources that the municipality is not able to utilize will be released and reallocated among the other municipalities that have fulfilled their material-financial execution requirements, following the procedures set forth in the Operating Regulations. The allocated amounts may also be released and reallocated if, within a six-month period from the signing of the framework agreement, the municipal government does not begin implementing the MAP.

4. Implementation

- 3.23 The financing commitment period will be three and a half years, counting from the effective date of the loan agreement. The term for disbursing the funds will be four (4) years, also from that date.
- 3.24 Upon signing of the framework agreement, the municipalities will initiate activities by contracting the necessary consulting services to prepare their respective MAP. The MAP must be submitted to INIFOM's approval and the Bank's no objection, and once approved, will be included as an integral part of the framework agreement.
- 3.25 The MAP must contain, at least, the following: (i) a detailed description of the institutional modernization activities required by the municipal government; (ii) description of proposed investments; (iii) activity schedules, (iv) progress and performance indicators; and (v) logical framework matrix.
- 3.26 The municipalities will carry out the other institutional modernization activities included in their respective MAPs. Access to the investment funds will be subject to the progress of the institutional modernization measured on the basis of attainment of the four targets as indicated in paragraphs 2.14 and 2.15. To avoid investments not made as a result of the failure to achieve the second set of targets, no projects designed by phases will be financed.
- 3.27 The municipality will contract, supervise and sign the certificate of approval and consent with respect to the consulting services required to formulate and implement the MAP, prepare the master urban development plan and conduct the investment project evaluations. To do so, it will follow the procedures set forth in the program's Operating Regulations.

- 3.28 The request to access the investment funds must be accompanied by evidence of attainment of the corresponding targets, evidence that the necessary counterpart funds are provided for in the municipal budget and evidence of the municipal government's commitment to collect fees or taxes to cover the costs of operating and maintaining the respective services, where applicable. The second request must include, in addition to the above-mentioned requirements, the submission of audited financial statements for the prior fiscal year.
- 3.29 Funds will go only to investment projects with technical, economic, financial and environmental feasibility studies. INIFOM must approve the preinvestment reports for each project proposed by the *municipios*, following the procedures established in the Operating Regulations.

5. Disbursements to the *Municipios*

- 3.30 INIFOM will disburse the funds through a revolving fund not to exceed 5% of the total funds allocated to each municipality. INIFOM will transfer the program funds to the bank account to be opened by the municipality in the name of Mayor's Office/IDB Program. Each municipality will also maintain a specific and separate account in which it will deposit the required local contribution, which account will be identified as Counterpart/IDB Program. The legal and operating aspects of the transfers and the payment thereof will be formalized in the framework agreements between INIFOM and the *participating municipios*.
- 3.31 The municipal governments will make their requests to INIFOM for disbursements subsequent to the first disbursement, and will have to submit the required supporting documentation of expenditures, according to the Bank's rules and regulations.

6. Monitoring and Supervision of the MAPs and the Investments

- 3.32 The municipal governments will have primary responsibility for monitoring the progress of the MAPs and the investments, and will contract consulting firms and/or individual consultants with the program funds. The municipal governments will require quarterly progress reports.
- 3.33 INIFOM will supervise the progress of the program activities and, for that purpose, will require quarterly material-financial progress reports. INIFOM and the Bank may make inspections at any time during the program.

7. Operation and Maintenance

- 3.34 All investments in municipal services will require the municipal government's commitment to collect fees and taxes to cover the costs associated with operating and maintaining such services. Any costs recovered must be allocated to the

institution or agency providing the services, which must be formed as an independent cost unit.

- 3.35 Maintenance of public works not subject to direct charges (such as the maintenance of drainage systems, green areas, urban roadways, etc.) will be the responsibility of the municipalities, as stipulated in the framework agreement.

E. Procurement of works, related goods and services, and contracting of consulting services

- 3.36 The procurement of goods and services will be in accordance with the Bank's policies. An international competitive bid will be required for contracts in excess of US\$1 million for construction works; US\$250,000 for related goods and services and US\$200,000 for consulting services. Works, goods and consulting services not exceeding these amounts will be subject to the procurement arrangement pursuant to the laws of Nicaragua, provided that they do not conflict with the Bank's procurement procedures.

- 3.37 The municipalities will procure the goods and services necessary to implement their respective MAPs and investments in accordance with the Bank's rules, through competitive processes. For contracts not exceeding the amounts mentioned in the preceding paragraph, the municipalities will apply the Law of Contracts with the State, provided that such provisions are compatible with the Bank's rules on the subject.

F. Disbursements and Revolving Fund

- 3.38 The program calls for the establishment of a revolving fund of 10% of the amount of the loan, inasmuch as several municipalities will begin activities at the same time and a sufficient revolving fund amount will be required so as not to delay the program's execution.

- 3.39 The loan proceeds and counterpart funds for Component 3 will be disbursed directly into a special bank account administered by INIFOM. INIFOM will consolidate all the data on execution and disbursements to the municipalities for Components 1 and 2, in order to submit its requests for disbursement to the Bank.

- 3.40 Given the nature of the operation and the anticipated volume of transactions for the procurement of goods and the contracting of services, INIFOM and the municipalities will maintain in their files originals and/or copies of the documentation justifying the use of the funds. This documentation must be properly identified and supplied to the authorized IDB officers and external auditors for inspection.

- 3.41 The IDB country office will make technical and financial ex-post inspections to examine the supporting documentation, including files and receipts of a random

sample of at least 10% of the projects. The inspection will verify that INIFOM and the local governments are maintaining in their files the disbursement request documents that show that the funds were used in accordance with the loan agreement. If there is a discrepancy in the required procedures, a broader sample will be examined and INIFOM will be notified of the amounts deductible from future requests.

3.42 The disbursement schedule will be as follows:

Source (in thousands of US\$)	Year 1	Year 2	Year 3	Year 4	Total
IDB	2,400	4,800	3,600	1,200	12,000
Local	600	1,200	900	300	3,000
Percentage	20%	40%	30%	10%	100%

G. Program monitoring

1. Monitoring and Evaluation

3.43 The program will be monitored and evaluated using the information provided by the project monitoring system used by INIFOM Department of Operations. The IDB project team and INIFOM management team will hold meetings every six months to review the program and evaluate the following: (i) procedures for promotion and inclusion of the *municipios*; (ii) progress of the performance indicators specified in the MAPs and their impact on the strengthening of municipal management and the effectiveness of coverage of services and infrastructure; (iii) progress of the material and financial performance of municipal investment projects; (iv) degree of progress with respect to institutional strengthening of INIFOM; (v) application of recommendations based on studies done in Component 3; and (vi) problems encountered and solutions adopted. These meetings will take place within 30 days following submission of the progress report by INIFOM.

3.44 The borrower, through INIFOM, will submit semi-annual progress reports to the Bank indicating the program's financial position, activities completed, products delivered and targets attained, as well as the major constraints encountered and solutions proposed. The report format should be agreed in advance with the Bank's country office.

2. Mid-Term Evaluation

3.45 The program will be evaluated in mid-term, 24 months into the program starting from the effective date of the loan agreement, or when 50% of the program funds have been disbursed, whichever occurs first. This evaluation will cover, among

other things: (i) attainment of the program's goals, measured by the management indicators proposed in the logical framework; (ii) attainment of the targets specified in the Municipal Action Plans, as set forth in the framework agreements and in the MAP logical framework matrixes; and (iii) enhancement of municipal T&TA services. The recommendations will be used to take the corrective measures, if necessary, to enhance program execution and ensure the attainment of its objectives. There will also be a final evaluation, after 90% of the program funds have been disbursed. Both evaluations must be conducted by an independent consulting firm acceptable to the Bank.

- 3.46 The government has agreed to submit annual evaluation reports for two years following the end of the program. These reports will follow the format of the semi-annual progress reports and will permit the Bank to obtain key information to refine the preparation, assessment and execution of new projects. Based on this agreement, and taking into account that the program provides for a mid-term and final evaluation, in addition to semiannual progress reports, the government authorities have declined to make an ex-post program evaluation.

3. Accounting and Audit

- 3.47 INIFOM and the municipal governments that will manage the program's funds will establish and maintain adequate accounts and records, in accordance with accepted accounting practices and will establish internal and independent control mechanisms to ensure compliance with the Operating Regulations. These accounts will be audited every fiscal year by a qualified independent auditing firm acceptable to the Bank. The audited financial statements that will be submitted to the Bank will include an opinion on the accounts and records and on the use of the program funds. The financial statements will be submitted to the Bank each year during the program.
- 3.48 In addition, INIFOM will contract, with the financing resources, the services of a consulting firm acceptable to the Bank to perform a program operations audit every six months, in accordance with the terms of reference agreed by INIFOM and the IDB. The operations audit will be aimed at reviewing, among other things, the following operating and financial aspects: (i) compliance with the requirements for program participation and access to investment funds; (ii) processing and compliance by INIFOM with the disbursement procedures set forth in the program's Operating Regulations, by reviewing a sample of the documentation accompanying the disbursement requests submitted to the Bank; (iii) compliance by INIFOM and the participating municipalities with the terms and conditions provided in the loan agreement and the program's Operating Regulations; (iv) compliance with the procedures of procurement and contracts under the program, by reviewing a sample of the documentation relating to the procurement of goods and contracting of works and services financed with the program funds; (v) compliance by the participating municipalities with the terms of the investment projects and quality guidelines, by

reviewing a sample of the projects executed with program financing; and (vi) use of the Revolving Fund by INIFOM and management of bank accounts by the participating municipalities.

IV. FEASIBILITY, ENVIRONMENTAL IMPACT, BENEFITS AND RISKS

A. Feasibility

- 4.1 INIFOM is an institution that manages and directs about US\$16 million annually in municipal investments, particularly to rural areas. Approximately 50% of these funds are executed using the institution's current administrative and financial structure (i.e., without resorting to an independent executing entity), and therefore it has working experience that will be quite valuable to the program. In any case, since the program activities are complex and will demand a high work load for INIFOM employees, resources have been provided in the budget for short-term consulting services to support the implementation and supervision of the program.
- 4.2 An analysis of the institutional and financial viability of Components 1 and 2 has concluded that the participating municipal governments: (i) have the capacity to make the institutional and financial assessment required to participate in the program; (ii) have the financial capacity to undertake the required local contributions; and (iii) can cover the operating and maintenance costs generated under the program.¹⁴ In addition, the program's execution cycle was assessed *vis-à-vis* the municipal electoral cycle. It was provided that this program's principal activities will be executed during the current local government administration, since the next municipal elections will be in the year 2004.
- 4.3 One of the program's goals is to increase investment planning at the municipal level. To do this, all investment projects financed under the program will have to have technical and economic feasibility studies to ensure that the project is the best solution to the problem to be resolved, and that the project will result in socioeconomic benefits. As part of the project selection criteria, these technical solutions should be cost-effective and comply with the requirement to exceed an EIRR of at least 12%, according to the Bank's policies. A consulting firm has been contracted to assist the *municipios* of the sample (Masaya, Rivas and Granada) in the identification and technical and economic evaluation of the proposed projects to ensure that they comply with technical and economic feasibility criteria.

B. Environmental and Social Impact

- 4.4 The program's strategy is to support the best land use planning and strengthen the municipal government's capacity to manage the environment and natural resources, while incorporating the environmental variable into the municipal project cycle.

¹⁴ In order to determine the *municipios'* ability to cover the local counterpart funds and operating costs of the program, financial projections were made, which established that the participating *municipios* will have to contribute not more than 30% of the real estate tax revenues to the program (assuming an incremental trend) without considering that this tax will substantially increase as a result of the program.

The program also provides that, in order to execute the investments, the *municipio* will have to attain a set of institutional modernization targets, one of which is the adoption of the Environmental Management System developed by the FISE with the Bank's support.

- 4.5 The program will have a positive social impact because it will introduce methods of participatory municipal planning that will result in urban development plans to control spontaneous settlements, and facilitate the planning and provision of local services and infrastructure. This will have a positive effect on the living conditions of the *municipio's* inhabitants in general, and specifically, those living in areas of urban expansion.

C. Benefits

- 4.6 The participating municipal governments will benefit from the program, since it will provide them with the technical assistance to strengthen their capacity to generate more revenue and modernize the management of municipal services. These governments will also have greater technical and financial means to cope with the challenges of urban growth and respond more effectively to the demand for local services and infrastructure. By the end of the program, the municipal governments will have strengthened their institutional and financial capacity, and will be better able to promote local development and deepen decentralization in Nicaragua.
- 4.7 In the perspective of strategies for municipal government modernization, this program will facilitate the introduction in Nicaragua of a model that conditions the access to investment funds on the adoption of municipal management reforms and sound practices. At the same time, the program will finance the implementation of a procedure, previously validated in other municipal programs (for example, in the municipality of San Pedro Sula, Honduras), based on providing comprehensive technical assistance and training in the core areas of municipal management, which are key to sustained improvement in institutional performance.

D. Risks

- 4.8 An increased turnover of personnel, on both the national and local levels, has been observed with the change of government administration. This is a risk to the program to the extent that the professionals and technicians trained in the next few years may be replaced by future administrations. The program seeks to mitigate this risk by increasing the technical value of municipal employees, which, in turn, will raise the cost to the municipality of replacing them. This added value will be possible through the professional training and technical assistance under the program and by the emphasis given to the adoption of municipal management methods, which require skilled personnel to execute them.

- 4.9 The risk under this program, caused by the possible replacement of INIFOM officials after the upcoming national elections, has been considered in two ways: (i) the program has been developed in consultation with municipal authorities that will have the influence to continue this initiative; and (ii) the Board of Directors of INIFOM will only have partial turnover because the municipal representative on the board, who fully understands the program's purpose, will remain the same.
- 4.10 The current ineffective coordination in the area of municipal training and technical assistance might be a risk if INIFOM does not coordinate the offer of technical assistance with the participating *municipios*. To reduce this risk, the following measures have been taken: (i) a logical framework workshop has been conducted in which the agencies that are funding projects with INIFOM have explained their programs and have discussed ways to achieve greater coordination of efforts; (ii) funds have been included for the design of a national technical assistance and training program, which will serve to provide assistance to the municipalities regardless of the provider; and (iii) the program will be managed within the municipalities by a modernization committee that, among its duties, will coordinate all implemented municipal institutional strengthening activities, regardless of the source of financing.

PROGRAM FOR MUNICIPAL STRENGTHENING AND DEVELOPMENT (NI-0156)

Logical Framework Matrix

Summary	Outcome Indicators	Verification Methods	Presumptions
Goal national and financial conditions for authorities of secondary cities to development	a. Municipal financial indicators and statistics.	INIFOM Statistics.	(general)
Purpose to strengthen institutional and of the municipal governments to cope with challenges of urban upgrade local services and	a.1. At least 10 municipalities have completed the RET catastro. a.2. At least 10 municipalities generate current savings. b.1. At least 10 services have independent cost centers. b.2. At least 20 municipal services have cost recovery. c.1. At least 10 municipalities have an environmental management plan approved by the Council. c.2. At least 10 municipalities have adopted the FISE Environmental Management System. d.1. At least 10 municipalities have Master Urban Development Plans (MUDP) approved by the Council. d.2. At least 10 municipalities have a semi-annual investment program. e. INIFOM has a national program for municipal T&TA, with a provider accreditation system.	a.1 Cadastral System (SISCAT) Report. a.2 Financial statements of municipality. b.1 and b.2 INIFOM MAP monitoring system. c.1. Minutes of Municipal Council. c.2. INIFOM MAP monitoring system. d.1. Minutes of Municipal Council. d.2. INIFOM MAP monitoring system. e. Program mid-term review and evaluation report.	Government support for decentralization and local development continues. The program's technical elements continue without political interference. The municipalities have the resources to make the counterpart contribution.
MUNICIPAL STRENGTHENING AND DEVELOPMENT (MAPs)			
m of training and technical signed and implemented.	a. At least 10 municipalities generate current savings and have completed urban cadastral surveys at program end. b. At least 20 municipal services have independent cost centers and 20 services recover operating and maintenance costs at program end. c. At least 10 municipalities have an environmental management plan and have adopted the environmental management system at program end.	INIFOM monitoring system and semi-annual reports from the participating municipalities.	At least 10 municipalities indicate an interest in participating in the program.

Summary	Outcome Indicators	Verification Methods	Presumptions
	d. At least 10 municipalities MUDPs and semi-annual investment plans at program end.		
INVESTMENTS			
es and infrastructure projects are cuted.	100% of the funds allocated according to specified criteria. 100% of the projects executed are identified in the Municipal Development Plans prepared according to INIFOM-FISE methods. 20% of the cost of the projects is contributed by the participating municipalities.	INIFOM project monitoring reports.	The municipalities have the resources necessary to make the local contribution.
STRENGTHENING OF THE INIFOM			
and technical assistance system is eration.	a. Accreditation system installed and operating by 6/2002. b. Municipal finance management system in operation by 6/2002. c. Tax management system in operation by 1/2003. d. Reengineering of regional agencies completed by 6/2003. e. Interinstitutional agreements signed and in execution by 6/2002.	Program monitoring and evaluation reports.	Staff turnover does not compromise execution of the program.
Activities	Resources	Verification Methods	Presumptions
Municipal Strengthening and Development (MAPs)			
ing of Management and Finances in Selected Municipalities MAPs and sign framework (<i>Municipio</i> –INIFOM) execute financial adjustment plans financial and administrative integrated finance management tax management system rules on procurement of goods and of services and works lastral survey execute training program	Component 1 Funds (US\$5.0 million).	Program accounting records for the entire component.	For all components: a. INIFOM has satisfactorily implemented the integrated systems of finance and tax management. b. Other agencies cooperate in the creation of strategic alliances. c. The Central Government maintains the political will to carry out the program. d. Each <i>municipio</i> is adequately coordinating activities with other projects. e. INIFOM key technical capacity is maintained throughout the program. f. Municipal authorities remain committed to the modernization of their institutions.

Summary	Outcome Indicators	Verification Methods	Presumptions
Summary of Municipal Services			
Alternatives of modernizing the delivery of services (outsourcing, privatization) Outsourcing projects and the creation of cost units by <i>municipio</i> Financed tax collection program Execute guidelines for quality operation	Component 1 Funds.		
Summary of Environmental and Natural Resource Management			
Environmental management unit to local level Environmental management system Implement environmental campaign Instruments for handling natural resources	Component 1 Funds		
Summary of Development Planning			
Update urban development plan Procedures for complying with urban development guidelines Project preinvestment studies Multiannual investment program Training department employees	Component 1 Funds.		
Investments			
Identify and execute works for selected projects.	Component 2 of US\$7 million.	Project accounting records and monitoring and supervision reports (INIFOM monitoring system).	
INIFOM Strengthening			
Training of municipalities to identify needs of demand for T&TA TA programs. Creditation system. Integrated financial management Municipal tax management system. Guidelines for procurement of goods and services and works with the municipality's own funds.	Component 3 of US\$2,562,000.	Program accounting records.	

**PROGRAM FOR MUNICIPAL STRENGTHENING AND DEVELOPMENT
PROCUREMENT OF GOODS AND SERVICES
NI-0156**

In thousands of US\$

Investment Category	Amount US\$	IDB (%)	LOCAL (%)
I. Municipal Strengthening and Development	5,000	4,000	1,000
1.1 Consulting Services	3,000	80	20
1.2 Equipment	500	80	20
1.3 Software licenses	250	80	20
1.4 Minor works	250	80	20
1.5 Training and instruction	1,000	80	20
II. Municipal Investments	7,000	5,600	1,400
2.1 Municipal works	7,000	80	20
III. INIFOM Strengthening	2,562	2,050	512
3.1 Consulting Services	2,100	80	20
3.2 Equipment	282	80	20
3.3 Minor Works	180	80	20

PROPOSED RESOLUTION

NICARAGUA. LOAN ____/SF-NI TO THE REPUBLICA DE NICARAGUA
Program for Strengthening Municipal Development

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 República de Nicaragua, as Borrower, for the purpose of granting it a financing to cooperate in the execution of a program for strengthening municipal development. Such financing will be for the amount of up to US\$12,000,000, or its equivalent in other currencies, except that of Nicaragua, which are part of the resources of the Bank's Fund for Special Operations, and will be subject to the "Special Contractual Conditions" and the "Financial Terms and Conditions" of the Executive Summary of the Loan Proposal.