

Local Development Program II

(ES-0120)

EXECUTIVE SUMMARY

Borrower:	Republic of El Salvador	
Executing agency:	Fondo de Inversión Social para el Desarrollo Local (FISDL)	
Amount and Source:	IDB: (OC)	US\$ 70.0 million
	Local:	US\$ 7.8 million
	Total:	US\$ 77.8 million
Financial terms and conditions:	Amortization period:	25 years
	Grace period:	5 years
	Disbursement period:	5 years
	Interest rate:	Variable
	Supervision and inspection	1% of loan amount
	Credit fee:	0.75 annually on undisbursed balance
	Currency:	Single currency facility
Objectives:	<p>The overall objective of the program is to improve the living conditions of poor people living in vulnerable municipalities and communities, using decentralized and participative methods that promote investments within the National Local Development Strategy. The specific objectives are to: (i) increase access of poor communities to basic services through the financing of social and economic infrastructure projects; (ii) build the capacity of municipal governments as well as community associations and non-government organizations to participate in sustainable local development processes; and (iii) strengthen the FISDL's normative and monitoring role of local development as well as its institutional management capacity.</p>	
Description:	<p>This program will support the government's reconstruction effort resulting from the two earthquakes of January and February 2001 within the framework of the ongoing local development process outlined in the ENDL and executed by the FISDL through the Local Development Program (PDL). It builds on the lessons learned from the IDB's ongoing operation which reconfirms that sustainable local development depends on capacity building of local actors, especially municipal governments, through a process of learning by doing.</p> <p>The proposed Program has three components: (i) Investments in priority social and economic projects; (ii) Capacity building of local actors; and (iii) Development of the FISDL's policy role and management capacity.</p>	

Component 1. Investments in social and economic infrastructure (US\$56,416,000)

In line with government priority to assist earthquake affected areas, eighty per cent (US\$45.1 million) of the investment resources will be allocated to reconstruction of basic economic and social infrastructure. These resources will be targeted to approximately 152 municipalities affected by the earthquakes--identified by their level of poverty and proportion of housing stock, health and education infrastructure destroyed.

The allocation of resources to these municipalities will use two mechanisms. A one-time amount will be earmarked ex-ante to each municipality using a sliding scale based on the percentage of housing destroyed and the damage to health and education infrastructure. The base of the scale will be US\$50,000 and its ceiling will be US\$150,000.

The second mechanism will be the competitive bidding mechanism used by FISDL. A municipality will be able to access these additional funds once it has fully committed its earmarked resources. FISDL will define groups of similar municipalities that will compete on an equal footing.

The remaining twenty per cent of financial resources available for investments (US\$11.3 million) will be allocated to approximately 86 poor municipalities (quintiles 1 and 2) using the competitive bidding mechanism. These municipalities were not affected by the earthquake, but have been historically marginalized from national development processes and have limited capacity to generate additional revenue. The FISDL will define groups of similar municipalities that will compete on an equal footing.

The approximately 24 municipalities that will not have access to investment resources comprise less poor municipalities (quintiles 3, 4 and 5) that were either not affected by the earthquakes or reported less than 10% destruction to their housing stock. These municipalities will have access to training and technical assistance resources to augment their financial, administrative and management capacity.

All municipalities will have to comply with basic eligibility criteria to access investment resources including: (i) the existence of a municipal development plan elaborated on the basis of a PPL process; (ii) evidence that the municipality has presented quarterly reports on the use of FODES resources to the corresponding entity; and (iii) evidence that the municipality is using its own resources to finance priority projects identified in municipal development plans elaborated using local participatory planning at

the municipal level (PPL).

Under the program the FISDL will continue its policy of responding to community driven demands and preferences. Three broad categories of eligible investments have been identified based on the PPL. Social projects, economic infrastructure projects and priority community projects. The FISDL will continue to apply its list of ineligible projects which will be monitored during program execution. All projects will have to be outsourced in order that municipal governments acquire experience in this area.

The program will also finance the replacement of municipal buildings declared inhabitable by the corresponding authority or destroyed in both cases by the earthquakes under the following criteria: (i) the investment has been prioritized in the PPL; (ii) a minimum cash counterpart by municipal authority of 50% of total project cost; and (iii) a maximum FISDL contribution of US\$100,000.

While the majority of investments will be managed by municipal governments, provision will be made for community associations and NGOs to compete in the bidding mechanism and execute investment projects.

Component 2. Capacity building of local actors (US\$7,050,000)

This component will finance technical assistance and training in the following areas:

Project formulation, supervision and sustainability (US\$1.0 million) The program will finance project formulation according to the technical guidelines established by FISDL. Assistance will also be provided for the development of sustainability plans covering project operations and maintenance and environmental considerations as well as tariff charges, where applicable. The program will strengthen the capacity of municipal authorities to supervise the execution of infrastructure projects.

Social Auditing (US\$500,000). The program will also finance activities to strengthen the capacity of community organizations to undertake oversight of project design, implementation and operation.

Municipal Participatory Planning (US\$2.2 million). The program will finance municipal governments to: (i) undertake municipal participatory planning (PPL) resulting in municipal development plans; (ii) build municipal capacity to institutionalize PPL processes; and (iii) revise existing municipal development plans. The package will be open to all 262 municipalities.

The PPL will be implemented according to agreed criteria to

ensure gender equity and equality, transparency and its institutionalization within municipalities. It will also incorporate additional criteria related to risk management and land use planning. The component will also finance PPL exercises between two or more municipalities associated in micro-regions.

Municipal Strengthening (US\$3,350,000).

- a. Municipal Financial Administration.** The sub-component will finance technical assistance and training to increase revenue generation and financial administration capacity with the objective of establishing creditworthiness. In addition the program will support the installation of municipal integrated financial administration systems in accordance with national norms, including the purchase of equipment and software.

The sub-component will benefit approximately 20 municipalities which will contribute no less than 10% toward the cost of the program. Municipalities will sign an agreement with FISDL, specifying program activities and benchmarks.

- b. Municipal Management Capacity.** The program will strengthen municipal capacity to manage and administer the decentralized project cycle, including the procurement and contracting of goods and services as well as the preparation and implementation of project sustainability plans. This program will also develop managerial capacity in areas such as human resource development, municipal information systems and inter-agency coordination at the local level. The FISDL will manage the outsourcing of the technical assistance provision; access will depend on the presentation of a technical assistance plan by a municipal government.

Component 3. FISDL's policy development and management capacity (US\$1.5 million)

This component will support the FISDL to strengthen: (i) its policy development and implementation capacity related to its role as lead agency in the execution of the ENDL; and (ii) its technical and administrative capacity.

The program will support: (i) the elaboration and execution of instruments, action plans and monitoring of capacity building related to municipal financial administration; (ii) the elaboration and monitoring of poverty targeting within PPL; and (iii) the development and introduction of risk management and land use planning tools into PPL.

The component will also provide funds to train FISDL's municipal advisors in accordance with their revised terms of reference. This will include PPL, municipal financial administration, gender

equity and equality, environmental impact assessment, bidding and contracting related to outsourcing, monitoring and evaluation of municipal capacity, project execution and sustainability plans, and social auditing.

The component will also augment FISDL's capacity to monitor and evaluate the impact of: (i) investments in social and economic infrastructure on the living conditions of the poor; (ii) technical assistance and training on the strengthening of the capacity of municipal governments and communities; and (iii) FISDL's performance as lead agency for ENDL and implementation of the PDL. This exercise will include the definition of base line data and indicators.

In addition, the component will support the FISDL to implement the recommendations of an Organization and Methods evaluation financed by the Bank, including: (i) revision of human resource strategy; (ii) revision of internal procedures, systems and manuals; and (iii) training of managerial staff.

The program will support the updating of the list of eligible providers of goods and services as well as pre-qualifying procedures. The component will also support the development and implementation of a social marketing strategy that will inform the wider public of their rights and responsibilities within the local development process. In addition, the component will support the strengthening of the institutional framework and operational relationships between the FISDL and ISDEM.

Other program costs (US\$270,000)

The program will also finance: (i) consultant services to assess and report on program advances for annual program reviews; (ii) annual external audits; and (iii) a mid-term evaluation.

Bank's country and sector strategy:

The Bank's strategy in El Salvador supports programs that: (i) promote economic growth and increase competitiveness; (ii) reduce poverty and develop human capital; and (iii) support state modernization and enhance governance. This strategy recognizes the importance of strengthening citizen participation, the building of government-civil society partnerships as well as the creation of broad political consensus behind key development programs. A priority area is support for the government's local development strategy and improvements in local public management and citizen participation mechanisms.

Environmental/ social review:

Environmental. The program will finance small scale social and economic infrastructure projects whose environmental impact is expected to be minimal. The FISDL has incorporated environmental issues in its policies and programs, and will build

environmental impact assessment capacity in municipalities. The program will support the elaboration and implementation of sustainability plans, which will include environmental considerations. It will also support incorporation of land use planning and risk management into the PPL and will provide technical assistance to municipalities to facilitate implementation.

Social Impact. The program will finance social and economic infrastructure projects that will benefit poor people. The program is designed to increase the participation and capacity of local actors in local development process. The PPL will improve the level of response to the priorities of poor populations, including those most affected by the recent earthquake. A basic principle of the program is to promote the equal participation of men and women in defining needs and priorities for local development in all phases of the project cycle and in the training activities undertaken locally.

Benefits:

The Program will allow municipalities to interact with their communities to make decisions about investments. This will ensure more efficient use of public resources. The program will support the earthquake reconstruction effort within the framework of the ongoing local development process. Poor municipalities not affected by the earthquake will also benefit with resources for investment and capacity building.

The capacity-building component of the program will result in municipalities becoming more competent in their core functions. The program will finance technical assistance and training to increase capacity of the largest municipalities in revenue collection and financial administration with the objective of making them credit worthy and will strengthen municipal management functions in all municipalities. The use of performance indicators to measure changes in municipal capacity during the program will allow FISDL to assess which types of technical interventions are most effective to order to adjust the packets of assistance accordingly.

Risks:

The risks associated with the capacity-building component have to do with the willingness of municipalities to participate, since their involvement is voluntary, and FISDL's promotion efforts to encourage their participation. The success of the financial strengthening component will be affected by the municipal fiscal framework. The success of the program also depends on the availability of a pool of service providers and on ensuring an equilibrium between the large increase in demand resulting from the program and the supply of adequate pre-qualified providers.

Special contractual clauses:	<p>Special conditions prior to first disbursement: Evidence that an agreement has been signed between the borrower and FISDL regarding the transfer of funds and the implementation of the program. (par. 3.1)</p> <p>The introduction of the program's operating regulations in accordance with the terms agreed with the Bank (par. 3.7).</p> <p>Other Conditions: The loan contract will contain other standard conditions, relating, among others things to monitoring and evaluation, audits, maintenance, procurement and contracting of services.</p>
Poverty-targeting and social sector classification:	<p>This operation qualifies as a social equity enhancing project, as described in the indicative targets mandated by the Bank's Eighth Replenishment (Document AB-1704). (Par. 4.21 to 4.23). Furthermore, this operation qualifies as Poverty Targeted Investment (PTI). (Par. 4.20). The borrower will be using the 10 percentage point in additional financing.</p>
Exceptions to Bank policy:	<p>None</p>
Procurement:	<p>All procurement under the program will be done in accordance with Bank rules. International competitive bidding will be required for construction of works in excess of US\$1.0 million, consulting services in excess of US\$200,000 and goods and related services in excess of US\$250,000. The minimum size of works that will be financed under the program will be US\$30,000. All works will be outsourced.</p> <p>Construction works, procurement of goods and related services and of consulting services of values below those requiring international competitive bidding will use the national contracting law (<i>Ley Nacional de Contrataciones y Adquisiciones del Sector Público</i>), provided it does not contradict the Bank's basic procurement principles.</p>

I. BACKGROUND

A. Socioeconomic context

- 1.1 Since the end of the armed conflict in 1992, El Salvador has established a sound basis for its economic and social development. The successful transition to peace and democracy has underpinned a period of strong economic growth averaging 4.6% per annum, low inflation--2.5% per annum over the last 3 years, and increased expenditures on health and education. As a consequence over the past decade, the numbers of poor fell from 60% to 41 %, illiteracy was cut from 30% to 17% and child mortality was reduced from 54 to 35 per thousand.
- 1.2 However, two major earthquakes of January and February 2001 caused extensive damage to the country's social and economic infrastructure of approximately US\$1.7 billion dollars. These disasters directly affected 1.5 million people, or 25% of the national population.¹ Over 189,000 houses were destroyed in 165 municipalities with a heavy concentration in 7 of the 14 departments.² In many cases, these dwellings doubled as places where people generated their family income. It is estimated that approximately 41,000 small and micro enterprises have been affected in this way. This situation is compounded by damage caused to social and economic infrastructure. For example, twelve percent of the country's schools were also destroyed and another 22% damaged, while 38 health units, or 12% of the national stock, were damaged.
- 1.3 It has been estimated that the earthquakes have increased national poverty levels by 2.4%, with an estimated 125,000 poor people being pushed into extreme poverty and the creation of 20,000 new poor.³ There are significant variations at the departmental level, however. For example, in Usulután, La Paz and Cuscatlán, poverty levels rose by an average of 7.0%, while in San Vicente, poverty levels increased by 13% from 65% to 78%. The result is that the country's poverty profile has been altered significantly since San Vicente has fallen from third poorest to become the poorest department, Usulután from fifth to third poorest and La Paz from seventh to fifth poorest.

B. Government Strategy on Poverty Reduction and Local Development

- 1.4 The present government that entered office in 1999 laid out its national development program in *La Nueva Alianza*, which identifies 4 *alianzas*⁴ that define strategic areas for action and partnership building in order to achieve the objectives of sustained economic growth, poverty reduction and effective participatory government. Within the *Nueva Alianza* framework, the Social

¹ These figures are taken from "United for El Salvador", the government's recovery plan presented to the Consultative Group meeting in Madrid in March 2001.

² Data collected by the local governments and processed by the FISDL.

³ FUSADES, "Efectos de los terremotos en la pobreza", mimeo, March 2001.

⁴ The four alianzas are the Alianza por el Futuro, Alianza Solidaria, Alianza por el Trabajo and Alianza para la Estabilidad Economica y Gobierno Efectivo.

Investment Fund for Local Development (FISDL) was given the responsibility for municipal development and strengthening, promotion of citizen participation in local development, resource transfer for local investment programs and to facilitate the integration of municipal governments into the national development process.

- 1.5 As a first step, the FISDL coordinated the preparation of a National Local Development Strategy (ENDL) with the support of a *Grupo Consultivo* comprising representatives of the public and private sectors.⁵ The ENDL forms a strategic part of the government's decentralization policy with respect to service provision at the local level. The overall objective of the ENDL is to promote an integrated process of local development supported by private and public institutions that addresses poverty and spatial inequality through decentralization, citizen participation and local capacity building. To achieve this objective, the ENDL identifies four operational areas: (i) reorganization of the institutional framework of public agencies; (ii) strengthened local development financing; (iii) increased investments in local level social and economic infrastructure; and (iv) introduction of environmental management and land use planning. The ENDL also identifies programmatic actions in each area as well as the roles of the different actors--municipal government, community associations, non government organizations (NGOs) and government agencies--in local development. The President of El Salvador endorsed the ENDL in December 1999, assigning to the FISDL the overall responsibility as lead government agency for coordinating and facilitating the implementation of local development policy.
- 1.6 The FISDL's has defined a Local Development Program (PDL) as its principal instrument to meet its responsibilities to promote local development within the framework of the ENDL. The objectives of the PDL are to strengthen the capacity of local development actors, especially municipal governments and communities, to carry out participatory planning processes, to manage a decentralized project cycle and to ensure project sustainability. In order to achieve these objectives, the FISDL finances activities that: (i) enhance the technical, financial and managerial expertise of municipal governments; (ii) promote citizen participation in local public affairs; (iii) increase resource mobilization for local development; and (iv) improve the sustainability and impact of local investments.
- 1.7 In addition, FISDL has embarked on a process to develop its capacity to elaborate public policy on local development using the experience gained from operational issues related to the PDL such as participatory planning at the local or municipal level (PPL) and decentralized project management.

⁵ The *Grupo Consultivo* comprises COMURES, the mayor's association, ISDEM, the Municipal Development Institute, the Red de ONGs, comprising 6 NGOs working in local development, and FUSADES, the Social and Economic Development Foundation, ANEP, the business association, *Secretaría Técnica de la Presidencia*, *Comisionado Presidencial para la Inversión Pública* and the Finance Ministry. The IDB, UNDP, USAID, GTZ and RTI have supported the Group.

- 1.8 A key instrument for financing local development is the Fondo de Desarrollo Económico y Social (FODES). This fund was created in 1988 to transfer annually financial resources to municipalities. In 1997 the amount transferred was increased from 2% to 6% of the national budget, equivalent to approximately US\$80 million annually. FODES funds are assigned to each municipality according to a formula that takes into account population size, municipal geographic extension, poverty and equity. These resources can be used for investments (80%) and recurrent expenses (20%).

C. Earthquake Reconstruction Strategy

- 1.9 A recovery plan from the damage caused by the two earthquakes is outlined in the document "United for El Salvador" presented by the GOES to the Consultative Group meeting of March 2001. This Plan identifies a reconstruction phase covering the period April 2001 to 2005. The main activities include the reconstruction of social infrastructure including schools, health centers, potable water and sanitation systems, rehabilitation of local roads as well as the strengthening of the administrative capacity of the local governments and participatory auditing mechanisms. This plan also highlights the need to develop national and local capacity in risk management related to natural disasters.
- 1.10 The Plan gives priority to those municipalities most affected by the earthquakes and also states that decentralization is fundamental to ensuring the participation of municipal governments and civil society in the reconstruction process. Municipal reconstruction projects will be identified on the basis of a consultative process between local actors and implemented using the decentralized mechanisms developed by the FISDL in the framework of the PDL, thus confirming the validity of the local development strategy for the reconstruction effort.
- 1.11 Commitments made at the Consultative Group Meeting, held in Madrid on March 7, 2001, included US\$1,376 million of which US\$399 million corresponded to donations from bilateral and multilateral sources, US\$267 million for the reformulation of existing loans and US\$710 million of new loans. The Bank's response to the two earthquakes included: (i) approval of two US\$50,000 technical cooperations for humanitarian assistance, (ii) approval of two emergency reconstruction facility loans of US\$20 million each, (iii) reformulation and reorientation of seven exiting loans for US\$107.3 million and (iv) approval of a US\$70 million tranche of the Modernization of the Public Sector loan to support the reconstruction program. The Government has created a coordination committee to promote the complementarity of reconstruction efforts. The FISDL is responsible for coordinating those efforts that will be implemented at the local level via a decentralized model of execution using municipal governments and communities. At the local level, the elaboration and revision of municipal development plans during the course of the next 6 months will help ensure that priority needs are identified. These plans will promote inter-institutional coordination between national and international agencies and facilitate the search for funding by municipal authorities.

D. The Fondo de Inversion Social para el Desarrollo Local (FISDL)

- 1.12 **Background.** The Social Investment Fund (FIS) was founded in 1990 as a compensatory fund to finance investments in small-scale social, economic and productive infrastructure using a centralized model of intervention. In 1996 it was restructured as the FISDL, a permanent agency with a mandate to “promote local development with the participation of municipal governments, communities, the private sector and central government institutions”. At this time, the IDB ceased to finance recurrent costs and the government introduced civil service terms and conditions for employees in order to establish the FISDL’s sustainability. The government continues to finance the institution’s recurrent costs.
- 1.13 **Bank Support.** Between 1990 and 1997, the Bank financed three operations with the FIS for US\$128 million. The main project types were schools (50%), sanitation (12%), environmental projects (12%), potable water (8%) and electricity (4%). In 1997, the Bank approved a US\$34 million operation designed to support two investment components. The first component was for financing projects in the pipeline previously identified under the FIS’s centralized way of working. The second component was to support the decentralization of the project cycle to municipal governments and the promotion of municipal participatory planning as the means of identifying priority projects in a sample of 30 municipalities. The loan also financed costs associated with the FISDL’s institutional transformation to its new role resulting from the implementation of a decentralized local development model, the PDL. The loan was declared eligible in November 1998 and to date 62% has been disbursed. Final disbursement is set for August 2002.
- 1.14 In early 1998, the context for program implementation changed when FODES transfers were increased from 2% to 6% (about US\$80 million annually) and the government decided to decentralize the responsibility for prioritizing projects remaining in FISDL’s project pipeline to municipal governments. The Bank agreed to the government’s request to tabulate program resources as part of FODES transfers for 1998 and 1999 on the understanding that these resources would be used according to the procedures established under the PDL. As a result, all program investment resources were allocated to support the introduction of the PDL into all 262 municipalities rather than as a pilot program in 30 municipalities. The effect on FISDL was to precipitate its reorganization in order to support the implementation of the decentralized project cycle on a national basis and to respond to an increase in municipal demand for technical assistance and training. In 2001, the FISDL has programmed the execution of US\$54 million under the PDL.
- 1.15 Alongside the implementation of the PDL model, the FISDL has continued to offer its services as an infrastructure executing agency (“FIS Industrial”) for the line ministries, especially the Ministries of Education and Health. Currently, the FISDL is contracted by the Ministry of Education to execute the IDB financed school infrastructure project. It is projected that in 2001 the FISDL will manage

US\$24 million under the executing agency modality. In addition, the FISDL has been the executing agency for the government's emergency housing program, executing approximately US\$60 million in close coordination with municipal governments.

- 1.16 **Lessons Learned from the PDL (1999 to 2001).** The ongoing program has shown that local governments and their communities are key actors in the government's decentralization policy. The government's post earthquake recovery plan reconfirms the central role of local actors in the reconstruction process over the short and medium term and that the PDL is a key mechanism to facilitate reconstruction within a decentralized framework.
- 1.17 Three main operational lessons learned from the experience of the PDL are: (i) that PPL is a valid means of promoting municipal government interaction with their constituent communities, but that its full potential has still to be realized; (ii) that municipal governments have proven capacity to manage a large volume of small-scale investment projects using the PDL's decentralized project cycle, but that they have yet to develop the capacity to fully outsource to contractors;⁶ and (iii) that improving investment management capacity must be complemented by strengthening other core functions to ensure sustainability.
- 1.18 With Bank support the FISDL has financed over 30 PPL exercises involving municipal governments, local communities and the private sector. These are in addition to ongoing efforts of other agencies--local and international non-government organizations (NGOs), public agencies such as ISDEM, bilateral agencies and UN agencies--that have introduced PPL into approximately 200 municipalities over the past 4 years. Although FISDL's participation in the promotion of PPL is more recent compared to other agencies this has nevertheless has allowed it to play a significant role in facilitating a much needed agreement with the Grupo Consultivo on national standards to be applied to PPL⁷. The experience in realizing agreement on the PPL basic criteria has shown the validity of this interactive process. This will permit a process of continual revision of these criteria as well as the introduction of new criteria, such as risk management and land use planning associated with the increased vulnerability of poor earthquake affected communities.
- 1.19 The municipal development plans resulting from PPL have improved the allocation of scarce resources to priority projects and are seen as the basis for

⁶ "El Programa de Desarrollo Local. Las Primeras Experiencias". Alejandro Bellegarrigue, Stephen Grun y Corina Mejia. Noviembre 2000.

⁷ The basic criteria were defined on the premise that each should contribute to the sustainability and institutionalization of PPL processes in order to identify community demands and obligations, to construct citizenship and support the democratization of local public life over the short, medium and long term with the overall objective of creating conditions that will lead to improvements in the quality of life of the population. The basic criteria are: sustainability, gender equity, inclusion of marginalized sectors, strategic vision, community responsibility, territorial and sector scope, transparency, facilitation of strategic alliances, continuity.

strengthening the coordination among different agencies operating at the municipal level. However, to ensure the sustainability of PPL and to realize its full potential as a mechanism for including marginalized groups in public policy decision-making, a series of actions are required, which include: (i) enhancing the capacity of communities and municipalities to undertake social auditing related to the implementation of the municipal plans and resulting project investments; (ii) the strengthening of the participation of women throughout the PPL and in the resulting project investments; (iii) the targeting of the poorest communities within the municipalities; and (iv) the periodic revision of the municipal investment plans.

- 1.20 The decentralization of the project cycle to municipal governments has resulted in the implementation of over 2,500 projects, of which 782 were financed with IDB resources, between January 1999 and May 2001. Of the total number of projects, 55% are road improvements 25% are electricity installation and 12% are in education. This distribution of project types differs sharply from that characterizing the previous operations with FIS--50% education; 12% sanitation; 12% environmental projects. This shift in project type reflects the use of a negative project list together with a bottom-up process of project identification and prioritization.
- 1.21 Project size averages US\$21,000, with 56% costing less than US\$20,000 and 7% costing more than US\$50,000. The large number of small projects has meant that nearly 80% of projects have been executed via direct administration by the municipal authorities. The external auditors conclude that the quality of projects completed to date is acceptable. However, they identify areas of room for improvement with respect to municipal supervision of project implementation, project maintenance and the keeping of project records.
- 1.22 Over the last 2 years, only 98 municipalities have had repeated experience of outsourcing. With Bank support the FISDL has initiated a process to increase municipal experience of managing the outsourcing of project execution. Outsourcing was introduced together with the assignment of resources by means of a national competitive bidding mechanism. This mechanism comprises a predetermined amount of available resources, predefined eligibility criteria⁸ and adjudication rules and procedures that are disseminated to all municipal governments via the media and the FISDL's municipal advisors. Only those municipalities that comply with the eligibility criteria can compete. Funds are adjudicated on the basis of (i) project type and (ii) the proportion of cash counterpart funding in relation to estimated project cost.
- 1.23 To date there have been 2 adjudications of funds via the competitive bidding mechanism, which have resulted in the participation of 87 municipalities and the earmarking of US\$8 million to finance 39 road improvement, water, education

⁸ These criteria are a PPL that complies with the 9 basic criteria and the liquidation of FODES funds for 1998 and 1999.

and electricity projects. The mechanism is perceived by the municipal authorities as a transparent and non-discretionary way of assigning financial resources which has resulted in higher than expected average cash commitments of municipal counterpart funding per project with an increase from 24% in the first round to 40% in the second. Over 70% of participating municipalities are poor (quintiles 1 and 2) and there is an increasing tendency for presentation of projects by groups of municipalities organized in micro-regions.

- 1.24 An initial analysis of the process indicates that municipalities of all types and sizes are entering the competitive process. However, one concern is whether smaller, poorer municipalities will be able to compete with larger richer municipalities. This concern points to the need to fine-tune procedures to ensure equity, so municipalities with similar characteristics, such as population size, management capacity, revenue and poverty levels, compete on an equal footing. The same analysis also indicates the need to revise procedures related to project pre-feasibility and feasibility studies in order to include aspects relating to social auditing, project maintenance and sustainability. A Bank financed evaluation is looking into these issues in more depth in order to identify and recommend the modifications required in the operating procedures.
- 1.25 **The Institutional Capacity of the FISDL.** The FISDL has restructured with Bank support its organization and structure to respond to its role as lead agency in local development and the decentralization of the project cycle. Two key changes are the creation of: (i) the post of municipal advisor; and (ii) the Research and Development Department (GID).
- 1.26 The FISDL has fifty-two municipal advisors who are the main point of interface with the 262 municipal governments, the FISDL's main client in the local development process. Initially, the advisors assisted with the introduction of the decentralized project cycle with its corresponding manuals and subsequently helped in the operationalization of the different procedures related to the project cycle such as administration, formulation, contracting, execution and liquidation.
- 1.27 Though a new and direct relationship has been established by the municipal advisors with the municipal authorities thus permitting a better knowledge of the municipal situation, additional training is required so that municipal advisors are better placed to provide a more effective response to municipal capacity building needs. The key areas to cover are project sustainability, social auditing, monitoring and evaluation of project impact as well as the promotion of the training and technical assistance services available to the municipalities under the PDL.
- 1.28 The establishment of the GID initiated the process of acquiring a new skills mix necessary to develop an institutional capacity in the areas of decentralization, PPL, and capacity building of local actors in order to support FISDL's role in local development as defined in the *Nueva Alianza*. Three significant results have been the preparation of the ENDL, the definition of the basic criteria constituting

PPL, and the development of a technical assistance and training strategy for developing local capacities.

- 1.29 Three areas identified by the FISDL that require immediate attention are: (a) municipal finance; (b) monitoring and evaluation and (c) organization and methods (O&M). In terms of municipal finance, the FISDL has identified the need to enhance its capacity on financial administration, revenue generation and municipal issues in general. Within monitoring and evaluation, critical strengthening is required around the impact of training and technical assistance on the capacity of local actors in such areas as social auditing, project management and sustainability, gender equity and equality as well as PPL. In addition, the FISDL recognizes the need to monitor its capacity to implement the PDL and promote policy development within the ENDL framework and to assess the impact of social and economic infrastructure projects.
- 1.30 An O&M analysis has reviewed the FISDL's internal systems and procedures in the areas of finance, administration, operations and personnel management. A series of recommendations in these areas have been made with the aim of ensuring that the FISDL is better positioned to meet its dual role as lead agency for local development and as execution agency for the Ministries of Health and Education.
- 1.31 **Project Sustainability.** There are three main groups of actors responsible for the projects financed under the PDL. These are public sector agencies such ANDA, the water and sewage agency, and the Health and Education Ministries (20%), private sector agencies such as the private electric distribution companies (25%) and municipal governments (55%). In the case of municipal authorities, the main project types are rural local roads⁹ and street improvements in urban centers.
- 1.32 While some mayors have established maintenance schemes and others have introduced tariffs and improvement charges stipulated by the Municipal Code, these efforts are not found in all municipalities. In order to ensure project sustainability of all project types, the FISDL is defining technical assistance and training packages to help design and implement sustainability plans that cover not only environmental considerations but also operation and maintenance costs. These will be included in project documents presented for financing by municipal governments. With respect to projects that do not clearly fall within the responsibility of one or another public or private agency, the challenge is to establish a mechanism that will identify the entity responsible for project operations and maintenance.

⁹ Local roads (*caminos vecinales*) are unpaved whose repair and maintenance is the responsibility of municipal governments. Rural roads (*caminos rurales*) are paved and unpaved feeder roads into the main arterial network. Their repair and maintenance is the responsibility of the Ministry of Public Works (MOP). The Bank's rural roads program (ES-0129) supports the network under MOP responsibility.

E. Municipal Governments in El Salvador

- 1.33 El Salvador is divided into 262 municipalities that are regulated by the 1993 Constitution and the 1986 Municipal Code. The Municipal Code establishes the judicial norms that define the competencies, functions and organization that govern each municipality. The Code identifies 28 competencies which include: (i) elaboration, approval and implementation of rural and urban development plans (art. 4.1); (ii) promotion of citizen participation in the solution of local problems (art. 4.8); (iii) protection of natural resources (art. 4.10); and (iv) planning, implementation and maintenance of municipal projects (art. 4.25). The Code also makes provision for municipalities to enter into associations with other municipalities in order to carry out projects as well as service provision that are of common interest (art. 11).
- 1.34 Municipal governments were first elected in 1985. Mayors and Council Members serve for 3 years and can stand for re-election. The most recent municipal elections were held in 2000. The Mayors are organized in a municipal corporation, COMURES that has become a key counterpart to FISDL in the definition and implementation of the PDL.
- 1.35 All municipal governments have demonstrated a capacity to manage basic project cycle responsibilities, which includes the receipt, use and reporting on financial resources and project implementation through direct administration. However, their ability to undertake more varied and complex tasks such as outsourcing and project sustainability, as well as other core municipal functions, depend on their installed technical capacity defined in terms of the presence of technical staff, the existence of technical, administrative and financial systems and procedures and their application.
- 1.36 The challenge ahead therefore is to design and implement a technical assistance and training package that can be tailored to the needs of individual municipalities and that will improve the quality of municipal management and financial administration as well as strengthen project management capacity. The result of a municipal typology study, now underway, will be the basis for developing a framework that will assist the FISDL in identifying the training and technical assistance requirements of each municipality.
- 1.37 Sustaining progress in building municipal technical capacity and processes of local development will depend on strengthening municipal finances. Currently, municipal income derives from two main sources. The first is income from municipal taxes, tariffs and special charges for improvements (e.g. urban street upgrading), and the second are transfers from central government through FODES. It is estimated that municipal tax income represents less than 1% of GDP and that FODES constitutes on average 90% of municipal income. Consequently, most municipalities are dependent on central government transfers to finance both investment projects and recurrent administration costs.

- 1.38 Among the most important constraints to increased generation of municipal revenue are: (i) lack of trained personnel; (ii) weak administrative and financial control systems; (iii) lack of property tax and under-utilization of available fiscal instruments; and (iv) lack of financial viability of many municipal services and works. Addressing this set of problems will require not only changes in the legal framework but also specialized technical assistance and training.
- 1.39 Under the ENDL, municipal governments have the role of promoting the development of inter institutional relationships with other local development actors. Although the experience of municipal governments working effectively with NGOs and community associations is limited, stronger links of this type are a key aspect of sustained local development processes and earthquake reconstruction efforts.

F. Coordination with other programs

- 1.40 The operation has been designed to support the local development program of the FISDL which was discussed and agreed at a logical framework workshop in September 2000 attended by IDB, World Bank, KfW, BCIE, Sida, GTZ and UNDP. This framework is also being used for the preparation of earthquake related programs as in the case of a US\$10 million KfW donation and a US\$2 million Sida donation. Preparation activities have been financed within the framework of the Sida-IDB Partnership for Central America.
- 1.41 The proposed program complements other Bank financed programs, specifically the rural roads rehabilitation project (ES-0129) and the housing program (ES-0087). The program will also prepare municipalities to access credit funds available under other programs such as the BCIE's municipal infrastructure program (PROMUNI).

G. The Bank Strategy

- 1.42 The Bank's strategy in El Salvador supports programs that: (i) promote economic growth and increase competitiveness; (ii) reduce poverty and develop human capital; and (iii) support state modernization and enhance governance. This strategy recognizes the importance of strengthening citizen participation, the building of government-civil society partnerships as well as the creation of broad political consensus behind key development programs. A priority area is support for the government's local development strategy and improvements in local public management and citizen participation mechanisms.

II. THE PROGRAM

A. Objectives

- 2.1 The overall objective of the program is to improve the living conditions of poor people living in vulnerable municipalities and communities using decentralized and participative methods that promote investments within the framework of the National Local Development Strategy. The specific objectives are to: (i) increase access of poor communities, especially those affected by the January and February 2001 earthquakes, to basic services through the financing of social and economic infrastructure projects; (ii) build the capacity of municipal governments as well as community associations and non government organizations to participate in sustainable local development processes; and (iii) strengthen the FISDL's normative and monitoring role of local development as well as its institutional management capacity.

B. Scope of the Program

- 2.2 This program will support the government's reconstruction effort resulting from the two earthquakes of January and February 2001 within the framework of the ongoing local development process outlined in the ENDL and executed through the PDL. It builds on the lessons learned from the IDB's ongoing operation which reconfirm that sustainable local development depends on capacity building of local actors, especially municipal governments, through a process of learning by doing. The program also reiterates the need to mainstream gender both into the PDL and the elaboration of local development policy.
- 2.3 The program will continue to support the PDL by placing greatest attention on three main themes: (i) strengthening the interaction between local governments and communities around the identification, implementation and operation of social and economic infrastructure projects; (ii) elevating the capacity of municipal authorities to manage local development processes in areas such as outsourcing, municipal finance, participatory planning, poverty targeting, gender and risk management; and (iii) incorporating the concept of project sustainability into project design.
- 2.4 The program will channel resources for investments in social and economic infrastructure as a means of promoting best practices. To this end, access to investment resources will be dependent on municipalities fulfilling eligibility criteria related to: (i) their commitment to a participatory process of local development as measured by the continued application of PPL; (ii) their capacity to account for FODES funds; and (iii) their commitment to allocate municipal funds to investment projects identified in municipal development plans. The program will make available resources for technical assistance and training at the local level not only to facilitate the attainment of these criteria but also to assist municipalities increase their revenue base and improve their financial management in order to establish credit worthiness.

- 2.5 The program is designed to work in all 262 municipalities with regard to building local capacities. Investment resources will be concentrated in approximately 152 municipalities most affected by the earthquakes in order to support the government's effort to respond to infrastructure reconstruction needs and to stimulate local economic activities with an influx of additional funds. Investment resources will also be available to poor and marginal municipalities not affected by the earthquakes. In addition, resources for the introduction of integrated financial systems will focus on 20 municipalities with greatest potential to access credit funds in the medium term.

C. Program Components

- 2.6 The proposed Program has three components: (i) Investments in priority social and economic projects; (ii) Capacity building of local actors; and (iii) Development of the FISDL's policy role and management capacity.

**1. Component 1. Investments in social and economic infrastructure
(US\$56,416.000)**

- 2.7 Based on the Government's priority to assist earthquake affected areas, eighty per cent (US\$45.1 million) of the financial resources available for investments will be allocated to construction, reconstruction and rehabilitation of basic economic and social infrastructure. These resources will be targeted to approximately 152 municipalities most affected by the earthquakes. These municipalities have been identified by their level of poverty and proportion of housing stock destroyed, as well as the damage caused to school and health infrastructure.
- 2.8 The allocation of resources to these municipalities will be based on two mechanisms. A one-time amount will be earmarked ex-ante to each municipality using a sliding scale based on the percentage of municipal housing stock destroyed and level of destruction to health and education infrastructure. The base of the scale will be US\$50,000 and its ceiling will be US\$150,000. These financial resources will be used to support projects identified in PPL. These municipalities will have up to 12 months to commit these funds; funds not committed will be reallocated according to the competitive mechanism described below.
- 2.9 The FISDL will initiate the second mechanism for allocating financial resources to the approximately 152 municipalities based on the competitive bidding mechanism used by FISDL under the current program. A municipality will be able to access additional funds by these means once it has committed its earmarked resources. For this purpose, FISDL will define groups of municipalities with similar characteristics that will compete for different tranches of funds.
- 2.10 The remaining twenty per cent of financial resources available for investments (US\$11.3 million) will be allocated to approximately 86 poor municipalities

(quintiles 1 and 2) using the competitive bidding mechanism. These municipalities were not affected by the earthquake, but have been historically marginalized from national development processes and have limited capacity to generate additional revenue. The FISDL will define groups of similar municipalities with similar characteristics that will compete for different tranches of funds.

2.11 The approximately 24 municipalities that will not have access to investment resources comprise less poor municipalities (quintiles 3, 4 and 5) that were either not affected by the earthquakes or reported less than 10% destruction to their housing stock. These municipalities will have access to training and technical assistance resources to augment their financial, administrative and management capacity.

2.12 **Eligibility Criteria.** All municipalities, irrespective of whether they are earthquake affected or not, will have to comply with four basic eligibility criteria in order to access all available financial resources for investments. These criteria are: (i) the existence of a municipal development plan elaborated on the basis of a PPL process complying with agreed basic criteria; (ii) evidence that the municipality has presented its quarterly report on the use of FODES resources to the corresponding entity; (iii) a certification from a certified auditor indicating that FODES funds for project investments have been used, and the accounts presented, for the period 12 months prior to the presentation to the FISDL of a request for financing under this program; and (iv) evidence that the municipality is using its own resources to finance priority projects identified in the local development plans elaborated using the PPL.

2.13 **Eligible Projects.** Under this program the FISDL will continue its policy of responding to community driven demands and preferences. Three broad categories of eligible investments have been identified based on the PPLs.

- a. Social projects such as school repair and the purchase of basic education equipment, health center repairs, water and basic sanitation.
- b. Economic infrastructure projects such as electricity, retaining walls, drainage channels, reforestation and local roads and other roads under municipal responsibility. The program will also finance markets under criteria of economic sustainability that will be agreed with the Bank.
- c. Priority community projects such as youth recreation facilities, village halls and creches for children of working parents.

2.14 The FISDL will continue to apply its list of ineligible projects: housing, municipal salaries and municipal equipment (outside that stipulated for municipal financial administration systems), credit for agricultural production and animal purchase, vehicles, religious and party political activities and buildings, fiestas patronales,

land purchase, and infrastructure and activities related to lottery and gambling schemes and highways.

- 2.15 The project team will evaluate the utility of the lists of eligible and ineligible projects during project execution.
- 2.16 All projects financed under this program will require the formulation of project files (carpetas técnicas) according to the technical guidelines of the program established by the FISDL. These will include, depending on project type, a pre-feasibility analysis that includes, technical, environmental and economic feasibility and any other required analysis. All projects will have a sustainability plan covering project operations and maintenance and environmental considerations as well as tariff charges where applicable. The project document will also indicate the cash contribution from municipal revenues and other sources towards project costs.
- 2.17 All projects will have to be outsourced so that municipal governments acquire experience in this area.
- 2.18 The program will finance the replacement of municipal buildings that have been declared inhabitable by the corresponding authority or destroyed in both cases by the earthquakes under the following criteria: (i) the investment has been prioritized in the PPL; (ii) a minimum cash counterpart by municipal authority of 50% of total project cost; and (iii) a maximum FISDL contribution of US\$100,000.
- 2.19 While the majority of investments will be managed by municipal governments, provision will be made for community associations and NGOs to compete in the bidding mechanism and execute investment projects. Local development actors will be required to demonstrate that they have their own legal status (personería jurídica). Prior to the participation of community associations and NGOs in this component, FISDL will present to the Bank for its approval, the terms and conditions, including eligibility criteria for their participation. These will form part of the Program Operating Regulations.

2. Capacity building of local actors (US\$7,050,000)

- 2.20 Technical assistance and training will be provided to communities and community associations to strengthen their participation in local development processes. This component will also provide financial resources for training and technical assistance for elected municipal officials and municipal employees in order to strengthen their capacity in two areas: (i) municipal financial administration and (ii) municipal management and administration.
- 2.21 **Project formulation, supervision and sustainability (US\$1.0 million)** The package of activities to be financed will include assistance to municipalities for project formulation according to the technical guidelines established by FISDL. These will include technical norms established by the respective line agency and

feasibility analyses taking into account project size and complexity. Assistance will also be provided for the development of sustainability plans covering project operations and maintenance and environmental considerations as well as tariff charges, where applicable. In addition, the program will provide assistance to increase the capacity of municipal authorities to review and assess the quality of project formulation; and to strengthen the capacity of municipal authorities to supervise the execution of infrastructure projects.

- 2.22 **Social Auditing (US\$500,000).** The program will also finance technical assistance and training activities to strengthen the capacity of municipal authorities to promote and facilitate social auditing. In addition, resources will be made available to strengthen the capacity of community organizations to undertake a mix of tasks that include: monitoring the project design, implementation, operation, maintenance and the use of funds. This component will also include the support of exchanges of experience between municipal authorities, organized community groups and their representatives in order to promote best practices in this area. Resources will also be available for civic communication on citizens' rights and responsibilities.
- 2.23 **Local Participatory Planning (US\$2.2 million).** The package of activities to be financed will include assistance to municipal governments to: (i) undertake local participatory planning (PPL) which will result in the elaboration of municipal development plans in municipalities without them; (ii) review existing municipal development plans; and (iii) strengthen municipal capacity to ensure the continued application of PPL. These activities will be carried out within the framework established by the basic criteria identified by the FISDL with the support of the Consultative Group. These include representativity, social and gender equity, amongst others. The PPL will also introduce additional criteria related to risk management and land use planning.
- 2.24 The PPL package will be open to all 262 municipalities. PPL will be carried out at the municipal level and coordinated by municipal governments and will receive technical and financial support from the FISDL, upon demand. PPL will include procedures to ensure participation of women and other excluded groups in project identification and prioritization. The PPL will also ensure participation of organized local actors, including NGOs, civil society organizations and private sector as well as representatives of central government agencies. The PPL will result in the definition of responsibilities, commitments and contributions of municipal authorities, communities and other local and central actors.
- 2.25 In those municipalities without municipal development plans, PPL exercises will typically have two stages that could be aided by external facilitators financed under the program. In a first stage, community level workshops will be held to identify problems, needs and alternative solutions. Participants will include members of the community and representatives of their organizations and special attention will be placed on ensuring the equal participation of men and women and marginalized groups as well as poverty targeting. This process will result in

an analysis of community problems, the prioritization of local needs and the creation of monitoring committees. In a second stage, workshops will be held at the municipal level with representatives from the monitoring committees, central government agencies, NGOs and municipal authorities. The outcome of this stage would be a municipal development plan that includes a consolidation of priority projects identified at the community and municipal level that will be funded by local revenue, FODES, PDL and other sources of funds.

- 2.26 The program will also support the revision of existing municipal development plans in order to ensure compliance with the existing basic criteria, the inclusion of criteria related to risk management and land use planning and an updating of priority projects. These activities could be aided by external facilitators financed by program resources upon request by municipal authorities.
- 2.27 With the aim of ensuring the continued application of PPL, the program will finance activities such as the training of local development committees (CODELs and CDLs) involved in the PPL process, training of municipal staff and local representatives, and the exchange of experiences between municipal authorities and community organizations.
- 2.28 The component will also finance participatory planning exercises between two or more municipalities associated in micro-regions based on watersheds or other criteria.
- 2.29 **Municipal Strengthening (US\$3,350,000).** In the area of **Municipal Financial Administration**, the program will finance technical assistance and training activities to increase municipal capacity in the areas of revenue collection and financial administration with the objective of making them creditworthy. The program will develop instruments to analyze municipal revenue potential and will support the implementation of action plans designed to realize this potential. The program will also support the installation of municipal integrated financial administration systems in accordance with national norms and will finance equipment and software. The package will be implemented in approximately 20 municipalities over the course of this program. Participating municipalities will make a cash contribution of no less than 10% towards the cost of the program.
- 2.30 In order to participate in the financial strengthening program, each municipality will agree ex-ante to a three-year technical assistance plan which will be outlined in an agreement covering aspects relating to: (i) cash counterpart contributions; (ii) commitment of counterpart human resources; and (iii) the definition of benchmarks which will be used to monitor municipal performance with regard to municipal financial strength, the introduction and maintenance of a system of financial indicators and the annual disclosure of their financial statements at the local level.
- 2.31 **Municipal Management Capacity.** The package of activities to be financed will address the strengthening of municipal capacity in the following areas: (i)

incorporation of a gender perspective in areas such as identification, planning and execution; (ii) poverty targeting of resources; (iii) financial audit training; (iv) procurement and contracting of goods and services related to project formulation and evaluation, execution and supervision; (v) risk management; (vi) municipal finance and administration; and (vii) service improvement. Resources will also be available to provide assistance to those municipalities wishing to create and/or strengthen micro-region associations as well as to promote exchanges between municipalities to disseminate lessons learned and good practices. This package will also support activities to improve the managerial capacity of the municipal authorities in areas such as human resource development, municipal information systems and inter agency coordination at the local level.

- 2.32 This technical assistance package will be available to all 262 municipalities upon demand and access to resources will require the presentation of a technical assistance plan, addressing the specific needs of the municipality, elaborated with the assistance of the municipal advisors. The plan will also identify the minimum 10% municipal contribution to the cost of the proposed training and technical assistance activities.

3. Component 3. FISDL's policy development and management capacity (US\$1.5 million)

- 2.33 This component will provide financial resources to the FISDL to strengthen: (i) its policy development and implementation capacity related to its role as lead agency in the execution of the ENDL; and (ii) its technical and administrative capacity to implement the PDL.
- 2.34 Long and short-term consultants will be contracted to strengthen the capacity of the FISDL in policy development and operational issues in the following areas: (i) the elaboration and execution of instruments, action plans and monitoring of capacity building related to municipal financial administration; (ii) the elaboration and monitoring of the use of poverty targeting at the municipal level within the framework of PPL; and (iii) the development and introduction of risk management and land use planning tools into PPL.
- 2.35 The component will also provide funds to train FISDL's municipal advisors on an ongoing basis in order to meet demand in line with their revised terms of reference. This will include PPL, municipal financial administration, gender, bidding and contracting related to outsourcing, monitoring and evaluation of municipal capacity and project execution and implementation of sustainability plans, conflict resolution and social auditing.
- 2.36 The component will also augment FISDL's capacity to monitor and evaluate the impact of the three program components: (i) investments in social and economic infrastructure on the living conditions of the poor; (ii) technical assistance and training on the strengthening of the capacity of municipal governments and communities in the areas of the application of the PPL, municipal financial

administration, municipal management capacity and social auditing; and (iii) FISDL's performance as lead agency for ENDL and implementation of the PDL. This exercise will include the definition of base line data and indicators. The development of monitoring and evaluation system will provide the inputs required for a strengthened management information system that will permit the FISDL to take informed decisions on a continual basis about the development and direction of the PDL.

- 2.37 In addition, the component will support the FISDL to implement the recommendations of an Organization and Methods evaluation financed by the Bank. Amongst the main areas are: (i) revision of human resource strategy including personnel policies, gender equity, contracting, career development and salary structures; (ii) the revision of internal procedures, systems and manuals; (iii) the training of managerial staff in managerial skills and techniques; and (iv) the development of the FISDL's internal communication systems.
- 2.38 The program will support the updating of the list of eligible providers of goods and services as well as the procedures to pre-qualify the providers and make them known to municipal authorities for their use. This exercise will also ensure that municipal authorities will be able to include local providers of services in these lists. The program will also support the updating of unit costs for prototype projects.
- 2.39 The component will also support the development and implementation of a social marketing strategy that will inform the wider public of their rights and responsibilities within the local development process. In addition, the component will help strengthen the institutional framework and operational relationships between the FISDL and ISDEM to ensure the complementarity of their actions in the implementation of the ENDL.

D. Other program costs (US\$270,000)

- 2.40 The program will also finance: (i) consultant services to assess and report on program advances for annual program reviews; (ii) annual external audits; and (iii) a mid-term and final evaluation.

E. Dimensioning of investment and capacity building component.

- 2.41 The size of the program's investment component is based on the effective demand from communities and the execution capacity of the FISDL and municipal governments. Experience with the PPL has shown it to be an effective instrument for identifying and organizing demand in conjunction with the communities themselves. In 23 PPL exercises supported by the FISDL priority projects for an amount of US\$39 million were identified, of which approximately 20% has been financed by resources available under FODES and from the FISDL. The damage caused from the earthquake has most probably increased the level of effective demand resulting in an increased resource gap.

- 2.42 Program execution capacity is based on the FISDL's proven capacity to disburse an average of US\$45 million per annum over the 1999-2001 period. The investment resources available under this program will finance projects greater than US\$30,000 in order to develop municipal capacity to manage outsourcing. Though this might result in a slower rate of disbursement over the short term, this is not expected to be a long term trend given the capacity of municipal governments to learn to manage project cycle procedures relatively quickly, the support that will be provided by the municipal advisors and the capacity of private contractors to execute expeditiously.

F. Cost and financing

- 2.43 Total cost of the program is estimated at US\$77,831,438, with IDB financing at US\$70,000,000 and will cover up to 90% of the programs total cost since this operation is geographically targeted, with a large proportion of investment and technical assistance resources earmarked for use in poor municipalities. Bank financing will also cover the interest during project execution.
- 2.44 Counterpart funds equivalent to US\$7,831,438, will come from the Central Government, in terms of support towards FISDL's institutional development and financial costs related to the loan. Counterpart funds could also include cash contributions from municipal governments and other participating actors towards the cost of investment projects.

(Thousands of US\$)

Components	IDB	Local	Total	%
Investments in social and economic projects	50,747	5,669	56,416	72.5
Social and economic infrastructure projects	50,747	5,669	56,416	
Strengthening of local actors	6,900	150	7,050	9.1
Formulation, supervision and sustainability	1,000		1,000	
Local participatory planning (PPL)	2,200		2,200	
Municipal financial and management capacity	2,400	100	2,500	
Social auditing	500		500	
Municipal financial administration systems	600		600	
Equipment and goods	200	50	250	
FISDL's policy development and management capacity	600	900	1,500	1.9
Technical assistance	600	527	1,127	
Training		238	238	
Equipment and goods		136	136	
Subtotal	58,247	6,719	64,967	83.5
Other Program Costs	270	0	270	0.3
Mid-term review	70		70	
External audits	200		200	
Financial Costs	11,483	1,113	12,595	16.2
Interest	10,783		10,783	
FIV	700		700	
Credit Commission		1,113	1,113	
Total	70,000	7,831	77,831	100.0
Percentage	90%	10%	100%	

Component totals are affected by rounding

2.45 The terms and conditions for the loan will be as follows:

Financing source	Ordinary Capital (OC)
Currency	Single currency facility
Terms:	
Amortization period	25.0 years
Grace period	5.0 years
Commitment period	4.0 years
Disbursement period	5 years
Interest rate	Variable
Supervision	1%
Credit Commission	0.75 per year on un-disbursed balance

III. ORGANIZATION AND ADMINISTRATION

A. Borrower and Executing Agencies

- 3.1 The borrower will be the Government of El Salvador. The executing agency will be the Social Investment Fund for Local Development (FISDL). **Evidence that an agreement for transferring the funds and implementing the program between the borrower and FISDL is in place is a condition prior to first disbursement.** This agreement should stipulate the conditions under which the loan and counterpart resources will be transferred to FISDL and the obligations assumed by FISDL regarding the execution of the program as agreed with the Bank.

B. Institutional Framework

1. The Social Investment Fund for Local Development (FISDL)

- 3.2 FISDL will be responsible to the Bank for implementing the program and will coordinate all activities related to its execution through its operational, financial and administrative departments. The FISDL's Technical Committee, comprising department heads and chaired by the Executive Director, will oversee the program implementation and report to the President. This Committee meeting monthly will ensure the: (i) monitoring and evaluation of program objectives; (ii) compliance with the program's operating regulations; (iii) efficient use of resources; (iv) timely preparation and submission of progress reports, including financial reports to the IDB; (v) maintenance of specific and separate commercial Bank accounts for the management of the program's funds; and (vi) dissemination of program activities to other program participants and stakeholders.

2. Other participating agencies

- 3.3 Municipal governments, community associations, NGOs and other specialized service providers (private firms and individual consultants) will participate in the execution of the proposed operation. The relations between FISDL and the participating agents, and between the different agents, will be established by respective contracts and agreements.

C. Inter-Institutional Coordination

- 3.4 The post-earthquake situation highlights the importance of strengthening coordination among actors in local development. The Consultative Group of FISDL has become a key forum where a wide range of actors discuss local development policies and programs and it is likely that it will continue to play this role in the foreseeable future.

- 3.5 The FISDL has coordination agreements with line ministries and other agencies, including the Ministries of Education, Health and Natural Resources, ANDA and local electric energy distributors, with regard to implementing technical norms for program execution and maintenance. The scope and content of these agreements will be revised to ensure that they correspond to the demands of the post-earthquake reality.

D. Program Execution

- 3.6 The program will be executed over a 4 year period, with 5 years to disburse resources. FISDL will transfer the program's resources to local governments on a non-reimbursable basis.

- 3.7 Program execution will be carried out in accordance with the Program Operating Regulations and its respective manuals and technical guides (guías técnicas) agreed between the IDB and FISDL. These regulations include: (i) mechanism for transferring funds to municipalities, procedures for managing bank accounts, and for accounting of the use of funds and procedures for deposit and use of cash counterpart contribution to project costs; (ii) bidding and procurement procedures for goods and related services purchased, the construction of civil works, hiring of service providers and eligibility criteria for goods and service providers; (iii) basic criteria for PPL activities; (iv) eligibility criteria for accessing investment resources, technical assistance and training; (v) rules and procedures that will be applied in the competitive bidding mechanism, including the mechanism to ensure targeting to the poorest and most vulnerable municipalities and communities, consistent with the Bank's PTI criteria; (vi) the content of the project technical file (carpeta técnica) in terms of technical, economic, legal, institutional, financial and environmental feasibility depending on project type; (vii) the format of the content of the sustainability plans required by each project; (viii) monitoring and evaluation system for measuring impact of investments in infrastructure, capacity building of local actors; (ix) the rules and procedures to be applied to the distribution of earmarked funds to earthquake affected municipalities; (x) the rules and procedures to be applied to the participation of community associations and NGOs in the execution of social and economic infrastructure projects; and (xi) the model of the contract between FISDL and the participating municipalities and community associations and NGOs for the execution of the different program activities. The updating of the operating regulations will include a gender perspective. **The introduction and implementation by the FISDL of the Program Operating Regulations agreed with the Bank will be a condition for first disbursement.**

1. Component 1. Investments in social and economic infrastructure

- 3.8 **Municipal authorities and employees** will: (i) lead participatory planning processes that result in the formulation of municipal development plans; (ii) manage the procurement of project formulators, evaluators, project contractors and supervisors, as well as the contracting of consultants and goods and services;

(iii) maintain separate bank accounts for investment and technical assistance projects financed by the program; (iv) maintain separate financial-accounting systems for funds from different sources; (v) maintain adequate files with all documentation related to each infrastructure project and each technical assistance and training service; (vi) present to FISDL the liquidation of project funds in a timely manner for each investment project and each technical assistance and training service; (vii) provide cash counterpart for investment projects; (viii) evaluate projects at all stages from the technical, financial, economic and environmental points of view; and (ix) present to FISDL each project file (carpeta técnica) with its respective sustainability plan.

- 3.9 Community associations and NGOs that fulfill eligibility criteria will also participate in the execution of investments in social and economic infrastructure.
- 3.10 **Community groups and their representatives** will: (i) participate in participatory planning processes, maintenance and social audits of works; and (ii) participate in local committees for execution of local development plans and execution, monitoring and maintenance of works.
- 3.11 **NGOs, individual consultants, public agencies and private firms** will provide specialized technical assistance and training to municipal governments, communities and to the FISDL.
- 3.12 **FISDL** will: (i) maintain and provide to municipal governments lists of authorized contractors and service providers; (ii) delegate the project cycle management to municipal governments; (iii) maintain and make available to municipal governments and contractors a complete and updated data base on unitary costs for building and maintaining prototype investment projects; (iv) verify compliance with all eligibility criteria; (v) verify that municipal governments have undertaken a technical, financial, economic and environmental evaluation of investments projects, and that each investment project includes an adequate sustainability plan; (vi) monitor the delegated project cycle, including progress of project execution, adequate use of funds and fulfillment of counterpart contributions and sustainability commitments; (vii) disburse program funds directly to bank accounts managed by local governments and ensure adequate use of funds; and (viii) verify that municipal governments maintain adequate filing systems that include original documentation on all transactions.

2. Component 2. Capacity building of local actors

- 3.13 **Municipal Authorities and employees** will: (i) receive technical assistance and training in: (a) participatory planning processes, including poverty targeting, gender, risk management and land use planning; and (b) decentralized project cycle management, including feasibility studies, sustainability plans and supervision; and social auditing; (ii) identify and make known to FISDL training and technical assistance needs in the areas of financial administration and management capacity, according to the procedures established in the program's

operating regulations; (iii) manage the procurement of technical assistance, training and equipment to strengthen their financial administration and internal audit capacity; and (iv) manage the procurement of technical assistance and training to strengthen their management capacity related to the incorporation of a gender perspective, procurement and contracting of goods and services, risk management, poverty targeting of resources, human resource development, and municipal information systems.

- 3.14 **Community groups and their representatives** will receive technical assistance and training in participatory planning processes--including how to apply a gender perspective--maintenance and social auditing of projects.
- 3.15 **NGOs, individual consultants, public agencies and private firms** will provide technical assistance and training in areas such as: (i) poverty targeting of resources; (ii) gender equity and equality and the promotion of the participation of women in local development; (iii) environmental and risk management, and land use planning; and (iv) training on municipal financial administration systems and municipal financial strengthening.
- 3.16 **FISDL** will: (i) maintain and make available to municipal governments an updated registry of pre-qualified consultants and contractors; (ii) maintain and make available to municipal governments an updated data base of costs of consulting services; (iii) brief its pre-qualified consultants and contractors on the procedures and norms of the PDL; and (iv) disburse program funds directly to bank accounts managed by local governments and ensure adequate use of funds.

3. Component 3. FISDL's policy development and management capacity

- 3.17 This component will be executed by FISDL, who will be responsible for contracting technical assistance and training to strengthen the capacity of its municipal advisors in areas such as PPL, gender equity, sustainability plans, bidding, contracting and acquisitions for outsourcing, poverty targeting, social auditing and management of decentralized project cycle. FISDL will also revise manuals and procedures related to personnel contracting, career development and salary structure.
- 3.18 FISDL will also contract technical assistance to: (i) strengthen its management information system and monitoring and evaluation of impact systems; (ii) to revise its information and communication systems with municipal governments other local actors; (iii) develop policy positions in poverty and local development, land use planning and risk management; and (iv) develop a system to monitor and evaluate the implementation of the sustainability plans. It will purchase equipment and software, develop and implement a training strategy for technical and managerial staff, and will also contract annual evaluations and annual external audits.

E. Procurement of Works, Goods and Consulting Services

- 3.19 All procurement under the program will be done in accordance with Bank rules. International competitive bidding will be required for construction of works in excess of US\$1.0 million, consulting services in excess of US\$200,000 and goods and related services in excess of US\$250,000. All works will be outsourced.
- 3.20 Construction of works, procurement of goods and related services and of consulting services of values below those requiring international competitive bidding will use the national contracting law (*Ley Nacional de Contrataciones y Adquisiciones del Sector Público*) provided it does not contradict the Bank's basic procurement principles.
- 3.21 Bank supervision for public bidding or other forms of procurement, if any, of works under US\$1.0 million, goods and related services under US\$250,000 and consulting services under US\$200,000 will be done ex-post, except for the first 3 biddings, which will be done ex-ante.

F. Disbursements

- 3.22 **Rotating Fund.** A rotating fund will be set up for the program. It is recommended to make it equivalent of 10% of the Bank loan available.
- 3.23 FISDL will present disbursement requests to the Bank to replenish the rotating fund following established procedures.
- 3.24 **Transfer Mechanisms.** The proceeds of the loan and government counterpart funds will be paid directly into a special bank account operated by FISDL. The transfers from the Government to FISDL will be done according to the terms and conditions stipulated in the resource transfer agreement that will be presented as a condition prior to first disbursement. The FISDL in turn will make transfers to named current accounts for each investment and technical assistance project to be managed by municipal governments and other participating agencies. The legal and operational aspects related to the transfers and their liquidation will be formalized in agreements between FISDL and the participating municipal authorities, and will be set out in detail in the program operating regulations.
- 3.25 The mechanism for transfer of resources will be as follows. On the basis of a satisfactory verification by FISDL of the project documentation presented by each municipal government according to the PDL's established norms and procedures, the FISDL will make the first disbursement equivalent to 33% of the total project cost to be financed by the FISDL. A second transfer of funds will be made to the project account when the municipal government satisfactorily liquidates expenditures made with the advanced funds. Subsequent transfers will follow the same mechanism. Final liquidation of expenditures will be made by the municipalities to the FISDL no later than 3 months after the last transfer is made. Each municipal government will deposit its cash project counterpart funds in the same named project account according to an agreed expenditure and disbursement

plan. The mechanism and procedures for transferring resources to community associations and NGOs will be agreed with the Bank and stipulated in the Program Operating Regulations.

- 3.26 Given the nature of the operations and the volume of transactions anticipated for the procurement of goods and hiring of services, the FISDL, municipal governments and participating community associations and NGOs will keep on file the originals and copies of all documentation needed to verify the use of program funds. This documentation will be duly identified and will be made available to authorized IDB officials and the external auditors for their verification.
- 3.27 The IDB's Country Office in El Salvador will carry out periodic ex-post technical and financial inspections of the disbursement's support documentation in accordance with the Bank's procedure, including project files and receipts related to a random 10% sample of investment and technical assistance projects. This will be the means of verifying that FISDL, municipal governments and other participating agents are maintaining documents supporting disbursement requests in their respective files, and that the funds were used as stipulated in the loan contract. In the event of discrepancies with respect to stipulated procedures being discovered, a broader sample will be examined and FISDL will be notified of any amounts to be deducted from future disbursement requests.
- 3.28 The disbursement schedule will be as follows:

Disbursement schedule

Year 1	Year 2	Year 3	Year 4	Year 5	Total
19%	21%	25%	25%	10%	100%

G. Accounting and External Audits

- 3.29 The FISDL, the municipal governments and participating community associations and NGOs will establish and maintain adequate accounting records, in accordance with accepted accounting practices, and will establish independent internal control mechanisms that guarantee compliance with the operating regulations.
- 3.30 An independent audit firm acceptable to the Bank, will be in charge of: (i) the semi-annual operational and financial audit of the program; and (ii) the annual audit of the program and the entity (FISDL). These audits will be performed under terms of reference previously agreed with the Bank. The audit costs will be financed by the Bank's loan funds.
- 3.31 The audit reports will be submitted by the FISDL to the Bank as follows: (i) within sixty (60) days after the closing of each semester for the semi annual audits; and (ii) within one hundred and twenty (120) days after the closing of the fiscal year for the annual audits.

H. Initial Report

- 3.32 The initial report presented by the FISDL to the Bank, will include annual action plans for each of the components. The initial report will also indicate how the FISDL will report on the monitoring and evaluation of the impact of program activities as well as progress in the introduction of gender into the program.

I. Monitoring, Evaluation and Reporting

- 3.33 **Monitoring and Evaluation.** The monitoring of program execution and evaluation of impact is the responsibility of FISDL, which will establish benchmarks to monitor implementation and to measure the progress of the program and its impact.
- 3.34 **Annual Reviews.** Annual reviews will consist of external reports and meetings between the FISDL and the IDB's Country Office in El Salvador. An external review of program in relation to annual action plans will be contracted by FISDL to start no later than 9 months after the loan has been declared eligible. The external reports together with progress reports and the annual review process itself will form the basis for defining the action plan for the second year. This annual review will be carried out no later than 11 months after the loan has been declared eligible . The action plan for the second year will be presented no later than one month after the conclusion of the annual review. This process will be repeated in the third year of program execution.
- 3.35 **Mid Term and Final Evaluations.** A mid-term evaluation will be held no later than 24 months after the start of program execution with the participation of the project team from Headquarters and Country Office, the FISDL and other program actors. The FISDL will contract consultant services, with terms of reference agreed with the Bank, to undertake this evaluation. The external evaluation together with progress reports and the mid-term evaluation process itself will form the basis for defining the action plan for the third year which will include any modifications or revisions to the program. A final evaluation will also be undertaken to measure the impact of the program. This evaluation will take place after program execution and prior to the last disbursement.
- 3.36 **Internal Reports.** The FISDL will submit six monthly reports, the form, scope and content of which will be agreed with the Bank's project team. These progress reports will be presented no later than one months after the closing of each semester of program execution.
- 3.37 **Bank Supervision.** The IDB's Country Office in El Salvador will be responsible for the supervision of program execution and will be supported by Headquarters, when necessary

IV. VIABILITY BENEFITS AND RISKS

A. Technical justification

- 4.1 The proposed program builds on the progress achieved to date by FISDL over the last three years in developing the PDL as a mechanism for promoting PPL and decentralized project cycle management, to facilitate sustainable local development within the framework of the ENDL. The government's recovery plan from the damage caused by recent earthquakes that have impacted the daily lives of 1.25 million people leading to increased levels of poverty in 10 of the country's 14 departments, has recognized the validity of these PDL mechanisms for ensuring the participation of municipal governments and civil society in the reconstruction effort.
- 4.2 This situation presents a series of challenges related to: (i) the consolidation of the decentralized local development model at a time when the country is reconstituting the social and economic fabric of those vulnerable, poor municipalities affected by the earthquakes; (ii) the improvement of living standards in other poor, marginalised municipalities not affected by the earthquakes; and (iii) the achievement of increased revenue and improved credit worthiness in the larger richer municipalities. The reconstruction effort will not only require investments in social and economic infrastructure but also the need to further strengthen the capacity of local government and communities to participate in the reconstruction and local development processes.
- 4.3 The program aims to assist the government in meeting these challenges by consolidating a series of actions already under way in the PDL in two broad interrelated areas: (i) development of technical assistance and training packages to be outsourced by FISDL to private and public agencies; and (ii) targeting of investment resources in poor municipalities.
- 4.4 The program will support the design and implementation of a series of technical assistance and training packages aimed at enhancing and strengthening local capacity in relation to their needs and demands. Among the results of this process are: (i) the design and implementation of sustainability plans for investment projects to ensure the overall feasibility of project operation and maintenance; (ii) the design and implementation of instruments to assist municipalities realize revenue potential and to enhance efficiency by means of the implementation of financial administration systems according to national norms; (iii) the institutionalization of the PPL exercise at the municipal level based on the continued application of basic criteria on a national scale, greater interaction between municipal governments and other local actors, participation of all sectors of local communities in definition, implementation and monitoring of municipal development plans, greater efficiency in the use of public resources and appropriation by means of the provision of greater counterpart resources; (iv) the introduction of risk management, land use planning and the improvement of targeting of resources to the poorest sectors of the municipal population in the

PPL exercise; (v) the development of additional skills and experience related to the management of the outsourcing project execution and the contracting of technical assistance and training; and (vi) the strengthening of community groups to undertake social auditing of project design, implementation and operation which will also enhance the quality of works.

B. Institutional Viability

- 4.5 The institutional viability of the operation rests on the experience of FISDL and its management team that has defined and implemented a process of institutional reorganization and restructuring over the past three years in line with its role as defined in the ENDL. The Government's endorsement of FISDL's role as lead agency for coordinating and facilitating the implementation of ENDL as well as the use of PDL methodology developed by FISDL for earthquake reconstruction as set out in the government's recovery plan, ensures institutional viability. Priority will continue to be given by the government to the development of FISDL's capacity to promote and facilitate sustainable local development and to the implementation of the PDL as its mechanism for ensuring the strengthening of local capacity to absorb processes and procedures decentralized by public agencies.
- 4.6 The program will cover the contracting of consultants to strengthen institutional expertise in the area of municipal financial administration and municipal revenue as well as the provision of resources to broaden the scope of the management information system in order to initiate the process of establishing a local development information system.
- 4.7 The program also recognizes that the strength of the FISDL lies in the quality of its people and that municipal advisors are a key resource. These advisors are the interface between the FISDL and its main client, the mayors, municipal authorities and municipal employees. Not only are these advisors central to the promotion of the services provided by FISDL but they are also a main source of information concerning the impact of the FISDL's local development program. The operation therefore provides the FISDL with the resources to invest in a program of ongoing training to realize the full contribution of the municipal advisors in meeting the development challenges that the operation proposes to the FISDL and the municipal governments.
- 4.8 The institutional viability of the program also rests on the capacity of the municipalities to build on their experiences as demonstrated by their ability, in the last three years, to receive, allocate and report on resources received in the framework of FODES and PDL.
- 4.9 The elaboration of the ENDL with the support of the Consultative Group indicates the positive contribution deriving from the interaction between public and private institutions with respect to public policy development. The scale and complexity of the reconstruction effort underscores the need to continue the development of

this, and other, mechanisms of interaction at the national and local levels in order to develop local capacity and to ensure the efficient investment of scarce resources. The program will continue to support coordination between national actors involved in local development as witnessed in the participation of COMURES, ISDEM and Red de ONGs in the definition of the logical framework of this program. In addition, the program will support inter-institutional collaboration at the local level around the elaboration and implementation of municipal development plans.

C. Financial Viability

- 4.10 The financial viability of the program stems from the Government's financing all of the institution's recurrent expenses. The Bank will not finance any recurrent cost of FISDL with regard to the PDL operation and related recurrent institutional costs. To this end, the program will enhance FISDL's capacity by means of the contracting of short and long term consultancies and the support of extensive training exercises especially of the managerial staff and the municipal advisors.
- 4.11 The financial viability of the investment projects will rest on the development of sustainability plans to be prepared by the municipal governments in the formulation stage and submitted to FISDL with each request for project financing. The program will make available to all municipal governments technical assistance and training packages to cover the technical, economic, financial, environmental aspects related to the preparation and implementation of these plans.
- 4.12 The financial viability of investment projects is further enhanced by the commitment of the municipal governments to provide a minimum of 10% cash counterpart funding per infrastructure project. In addition, the financial viability of each PPL exercise will be enhanced not only by means of a technical assistance and training package offered to all municipal governments but also the commitment of the participating municipalities to program and use its own revenue, in addition to its cash counterpart contribution to infrastructure projects, to finance projects identified in the municipal development plans resulting from each PPL exercise.

D. Environmental Viability

- 4.13 The FISDL has incorporated environmental issues in its policies and programs, and through the presentation of sustainability plans for each infrastructure project will build environmental impact assessment capacity in municipalities. Financial resources will be available to assist municipalities elaborate the respective sustainability plans, including environmental considerations. The program will support the revision of project related environmental norms and their implementation by municipal governments to ensure the environmental feasibility of program investments.

- 4.14 The program will also support the incorporation of land use planning and risk management into the PPL and will provide technical assistance to municipalities to facilitate implementation. By building capacity in land use planning and risk management, the program will assist municipalities develop their ability to identify the environmental protection measures required to address project environmental impact.

E. Benefits

- 4.15 The Program will allow municipalities to work together with their communities to make decisions about investments in social and economic infrastructure. The program will support the earthquake reconstruction effort within the framework of the ongoing local development process by providing resources for investments in social and economic infrastructure, as well as capacity building. Poor municipalities not affected by the earthquake will also benefit with resources for investment and capacity building. Municipalities with greater potential will benefit from technical assistance and training packages to enable them to increase their revenue base and access credit in the medium term.
- 4.16 The capacity-building component of the program will result in municipalities becoming more competent at some of their most important core functions. The systematization of the capacity-building process through the development of guidelines and packets will result in a more efficient system in which fewer resources are used to prepare to deliver the training and technical assistance and more can be used on the actual strengthening activities. By strengthening the finances of the stronger municipalities, the municipal finance component will allow FISDL in the future to better focus available resources in the poorer municipalities. The use of the performance indicators to measure changes in municipal capacity during the program will mean that FISDL and the TA providers will be able to better understand which types of technical interventions are most effective, in order to adjust the packets of assistance in the future.

F. Risks

- 4.17 The risks associated with the capacity-building component have to do with the willingness of municipalities to participate, since their involvement is voluntary, and whether FISDL's program to encourage their participation will produce enough of a response that the program will have a measurable impact.
- 4.18 The success of the financial administrative strengthening component will be affected by the municipal fiscal framework. The passage of the local property tax, which has recently been the subject of considerable political debate, has been postponed until at least next year due to the earthquake. Fiscal strengthening can take place based on better use of other existing fiscal instruments, but the impact of the component will be greater if the property tax is available to municipalities as a fiscal instrument. However, once municipalities are credit worthy the risk exists that suitable sources and forms of credit may not be available in the private market.

- 4.19 The success of the program also depends on the availability of a pool of service providers of technical assistance and training to municipal governments and communities. Although, the implementation of the PDL has helped to create a market for service providers and a more diversified range of service providers with a wider range of skills and expertise, the impact of the technical assistance and training packages will largely depend on ensuring an equilibrium between the very large increase in demand resulting from this program and the supply of adequate service providers.

G. Social equity and poverty targeted investment

- 4.20 This operation qualifies as a project that promotes social equity as defined in the Banks Eighth Replenishment (Document AB-1704) and as a poverty targeted investment (PTI). All investment resources of the Program and a large proportion of resources for technical assistance and training have been earmarked for use in poor municipalities (quintiles 1 and 2) or those badly affected by the earthquake in order to improve the provision of basic services and to strengthen the capacity of local actors.
- 4.21 **Social Impact.** The program is designed to increase the participation and capacity of local actors in local development process. The PPL will improve the level of response to the priorities of poor populations, including those most affected by the recent earthquake.
- 4.22 The program will target investment resources to poor vulnerable municipalities for social infrastructure projects and basic services. By ensuring access to basic services of education, health, electricity, water and sanitation as well as to markets by improving local roads, the program resources will have an impact on the living standards of a substantial number of poor people especially those living in rural areas. The investment resources will also be used as incentives for the introduction and consolidation of best practices in municipal governments particularly in the areas of PPL, project management and sustainability.
- 4.23 The program components contain elements to increase women's participation and to promote gender equity and equality in local development processes. This will be ensured through the greater responsiveness in social auditing and PPL to priorities of women, as well as the training of municipal governments in gender awareness and the training of women as members of the different local monitoring committees. The aim is to ensure not only increased participation of women but also to promote gender equity and equality. This process will be aided by an evaluation currently underway of the impact of the gender policy and its recommendations will be incorporated into the program. In addition, a complete review of the procedures and norms of the PDL will be realized by FISDL from the perspective of promoting and ensuring the participation of women, and gender equity and equality.

EL SALVADOR
LOCAL DEVELOPMENT PROGRAM II (ES-0120)
LOGICAL FRAMEWORK

	Indicators	Means of Verification	Assumptions
			Sustainability
living conditions at the local level, balanced approach to cover the whole	1.1 80% of the investment resources targeted at municipalities affected by earthquakes by end of project 1.2 20% of investment resources targeted at poor municipalities (quintiles 1 and 2) by end of project		
			Purpose to Goal
ole use of higher quality economic services provided through a decentralized and coordinated mechanism public and private agents in the communities	1.1 Rate of coverage of basic social services and infrastructure provided through a decentralized and coordinated approach, by sector, increases to at least 50% at the national level and at least 50% in extremely poor municipalities by end of project 1.2 At least 75% of works and services maintain their level of quality three years after delivery, with maintenance provided by local agents who received training by end of project.	1.1.1 SIG FISDL 1.2.1 Monitoring reports and final report	Other complementary projects are successfully executed El Salvador is able to maintain its comparative trade advantage in the context of sustained growth and fiscal stability.
Interventions			Components to Purpose
Investments in priority social and economic infrastructure projects executed	1.1 At most 1,275 socioeconomic projects >US\$30,000.00 priorities through the municipal participatory planning (PPL) process, with sustainability plans adopted and with a contribution of at least 10% in cash 1.2 100% of projects presented to FISDL for financing have sustainability plans	1.1.1 Monitoring and evaluation system and FISDL technical reports 1.4.1 Project files	At least 75% of trainees use new skills. Draft laws are approved by Legislative Assembly.
Program to strengthen institutional capacity of local actors designed and executed	2.1 TA provided for the establishment of 10 associations of municipalities by end of project 2.2 Inter-institutional public access information system designed and in operation by end of project 2.3 80% of municipalities trained in PPL incorporating the concept of land use planning and risk and environmental management by end of project. 2.4 Training provided to 80% of the community groups, project committees and civil society organizations participating in the program in areas of project management, social auditing, and operation and maintenance by end of project	2.1.1 List of participating municipalities and FISDL technical reports 2.2.1 FISDL's MIS 2.3.1 List of participating municipalities and FISDL monitoring reports 2.4.1 List of participants, records of training courses, and FISDL technical reports	

	Indicators	Means of Verification	Assumptions
	<p>2.5 In the municipalities that implement projects (component 1), a civic education program on citizens' rights and responsibilities has been developed by end of project</p> <p>2.6 Municipal credit rating system defined and applied in at least 20 municipalities by end of project</p> <p>2.7 Instruments to measure revenue collection potential defined and applied in at least 60 municipalities by end of project</p> <p>2.8 Strategies for municipal revenue collection defined and implemented in at least 30 municipalities by end of project</p> <p>2.9 Integrated Financial Administration Systems (SIAF), in accordance with national norms, installed and operating in at least 20 municipalities by end of project</p>	<p>2.5.1 Records of training sessions, list of participants, and FISDL technical reports</p> <p>2.6.1 Final report on definition work and municipal rating reports</p> <p>2.7.1 Final report on design of instruments; semiannual FISDL report; biannual reports and financial statements from 60 municipalities</p> <p>2.8.1 Final report on strategies; semiannual FISDL report on collection program, consultants' reports and work plans; biannual reports and financial statements from 30 municipalities</p> <p>2.9.1 Biannual report, national group of municipalities with SIAF; biannual FISDL report</p>	
<p>grams to strengthen FISDL in the ution of public policies related to national local development strategy (IDL) designed and implemented</p>	<p>3.1 Proposal to adjust the legal and institutional framework of the ENDL presented to respective authorities by June 2003</p> <p>3.2 Proposal to amend current legislation to ensure opportunities for citizen participation in local development processes presented to respective authorities by December 2003</p> <p>3.3 Training and development program on decentralization, local financing, legal and institutional framework, citizen participation and consultation for institutions involved in the ENDL designed and executed by end of project.</p> <p>3.4 ENDL social communication strategy designed and implemented by December 2002</p> <p>3.5 Proposal to change the institutional framework for municipal financing and outsourcing of services prepared by December 2003 and presented to authorities</p> <p>3.6 National rules for integrated financial administration systems defined</p>	<p>3.1.1 Proposal drafted and under consideration by respective authorities</p> <p>3.2.1 Proposal drafted and under consideration by respective authorities</p> <p>3.3.1 Annual monitoring reports and final report</p> <p>3.4.1 Communication strategy document and annual monitoring reports</p> <p>3.5.1 Final proposal of reform plan drafted and under consideration by respective authorities; semiannual FISDL report on reform program</p> <p>3.6.1 National rules published; semiannual FISDL report (GID)</p>	

	Indicators	Means of Verification	Assumptions
	Inputs/Resources		Activities to Components
<p>prepare project files</p> <p>verify fulfillment of qualification requirements</p> <p>for bids on projects</p> <p>transfer resources to municipal governments</p> <p>execute</p> <p>revise and terminate</p>	Budget		<p>Response capacity to natural disasters allows investment to continue.</p> <p>Resource transfers to municipalities continue and are executed transparently.</p>
<p>establish criteria for participatory processes</p> <p>develop participatory processes including sustainability and investment</p> <p>identify TA needs in social auditing</p> <p>create a bank of facilitators</p> <p>design curriculum</p> <p>train trainers</p> <p>transfer resources for training</p> <p>in</p> <p>identify opportunities and need for associations of municipalities</p> <p>design TA program and training</p> <p>transfer financial resources</p> <p>implement</p> <p>evaluate</p> <p>identify demand and needs</p> <p>design TA program</p> <p>provide equipment to implement systems</p> <p>in</p> <p>implement and evaluate</p> <p>identify demand for information at local level</p> <p>design information system</p>	Budget		

	Indicators	Means of Verification	Assumptions
<p>Secure equipment</p> <p>Implement system and evaluate</p> <p>Identify demand and needs</p> <p>Design program</p> <p>Transfer resources</p> <p>Implement and evaluate</p> <p>Design system to qualify municipalities</p> <p>Test instrument</p> <p>Select municipalities for evaluation</p> <p>Apply qualification system in municipalities and disseminate results</p> <p>Test instrument</p> <p>Design instrument to measure municipal revenue potential</p>			
<p>Test instrument</p> <p>Select municipalities for instrument qualification</p> <p>Apply the system to measure municipal revenue potential and disseminate results and instrument</p> <p>Refine concept for municipal collection strategy</p> <p>Select municipalities for strategy development</p> <p>Develop strategies for revenue collection in municipalities</p> <p>Support municipalities in carrying out strategies</p> <p>Evaluate results</p> <p>Develop national guidelines for the FIMU system</p> <p>Select municipalities for system installation</p> <p>Install SAFIMU systems in municipalities</p> <p>Provide training to municipal officials</p> <p>Ensure proper use of the systems</p>			

	Indicators	Means of Verification	Assumptions
luate results lyze institutional framework pare institutional framework reform velop work plan to implement ecessary institutional reforms			
view legal and institutional network pare preliminary proposal onsult stakeholders ft and present proposal nduct diagnostic assessments of ls and existing supply sign training program lement training nitor and evaluate sign communication strategy lement luate results	Budget		

PROCUREMENT PLAN

Main Procurement	Financing	Procurement Method (US\$)	Pre-qualification	Expected SPN Publication date
Program administration				
Short-term consultancies (US\$270,000) Annual and mid-term reviews External audits	100 % IDB	ICB greater than US\$200,000 NCB Between US\$28,801 and US\$200,000 LCB Less than US\$28,800	No	I/2002 To II/2005
Equipment, goods and related services (US\$95,000) Upgrading existing system Implementation Intranet system Implement Data Warehouse	100% GOES	ICB greater than US\$250,000 NCB Between US\$91,441 and US\$250,000 LCB Less than US\$91,440	No	I/2002 To II/2005
Program Execution				
Short and long-term technical assistance (US\$6,826,500) Finance and administration: budget and programming, project administration, contracting and acquisitions, municipal information systems, reengineering of management information systems, human resource management, conflict management and team work. Service and local development: operation and maintenance of services, concession of services, service regulations, implementation of tariff systems, local and regional economic development. Municipal Legal framework Strengthen FISDL's institutional management, personnel, contracting, career development and salary structure. Develop and or strengthen managerial skills Incorporate information technology Implement intranet system, knowledge management, document administration and internal communication. Design information system modules Implement Data Warehouse system for decision making Develop system to facilitate transfer of technology to municipalities 1. Municipal finance advisor 2. Studies: municipal finance legal framework, information systems, information diffusion strategy, harmonizing of norms, instruments and policy and program proposals	91% IDB 9% GOES and Local	ICB greater than US\$200,000 NCB Between US\$28,801 and US\$200,000 LCB Less than US\$28,800	No	I/2002 To II/2005

Main Procurement	Financing	Procurement Method (US\$)	Pre-qualification	Expected SPN Publication date
3. Technical studies relative to: Poverty and local development, risk management and land use planning. 4. Promotion and communication to local governments; 5. Develop educational and social communication strategy. 6. Strengthen monitoring and evaluation system 7. Elaborate manual and guides for municipal governments to use in the development of sustainability plan. 8. Strengthen municipal asociatividad into micro regions. 9. Municipal Planning processes 10. Project formulation, supervision and sustainability 11. Other technical assistance				
Training (US\$1,338,000) . Municipal governments in use of municipal financial administration system. . FISDL management team . Municipal Advisors . Exchanges, workshops, etc. . Training in project and municipal auditing	82% IDB 18% GOES and Local	ICB greater than US\$200,000 NCB Between US\$28,801 and US\$200,000 LCB Less than US\$28,800	No	I/2002 To II/2005
Equipment, Goods and related services (US\$290,500) . Computer and software for municipal financial administration system . Web system. Transfer of technology from FISDL to municipal governments. . Monitoring and evaluation system	69% IDB 31% GOES and Local	ICB greater than US\$250,000 NCB Between US\$91,441 and US\$250,000 LCB Less than US\$91,440	No	I/2002 To II/2005
Investments in social and economic projects				
Investments (US\$56,416,000) . Social and economic projects	90% IDB 10% Local	ICB greater than US\$1,000,000 NCB Between US\$91,441 and US\$1,000,000 LCB Less than US\$91,440	No	I/2002 To II/2005
B International competitive bidding CB National competitive bidding B Local competitive bidding N Special Procurement Notice				

PROPOSED RESOLUTION

**EL SALVADOR. LOAN No. ____/OC-ES TO THE REPUBLICA DE
EL SALVADOR**

(Local Development Program II)

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 El Salvador, as Borrower, for the purpose of granting it a financing to cooperate in the execution of a Local Development Program II. Such financing will be for the amount of up to US\$70,000,000, from the resources of the Single Currency Facility of the Bank's Ordinary Capital, and will be subject to the "Financial Terms and Conditions" and the "Special Contractual Conditions" of the Executive Summary of the Loan Proposal.