

MUNICIPAL INSTITUTIONAL-DEVELOPMENT AND SOCIAL-INVESTMENT PROGRAM

(AR-0058)

EXECUTIVE SUMMARY

BORROWER AND GUARANTOR: Argentine Republic

EXECUTING AGENCY: Secretaría de Desarrollo Social [Department of the Secretary of Social Development] (SDS) of the Office of the President

AMOUNT AND SOURCE:

IDB:	US\$180,000,000 (OC)
	US\$ 30,000,000 (FSO-local currency)
Local contribution:	US\$ 90,000,000
Total:	US\$300,000,000

FINANICAL TERMS AND CONDITIONS:

Amortization period:	25 years
Disbursement period:	6 years
Grace period:	6.5 years
Interest rate:	variable (OC)
	4% (FSO)
Inspection and supervision:	1% of the loan
Credit fee:	0.75% of the undisbursed balance (OC)

OBJECTIVES: The general objective of the program is to support the municipalities in their actions to improve the quality of life of their residents, particularly those belonging to low-income groups, and the federal government in its policy to decentralize public finances and place them on a sound footing.

DESCRIPTION: The program will include an institutional development component and a works component. The institutional development component (US\$20 million) will be composed of two closely-related subcomponents:

- a. A municipal situation study (MSS), to be performed in each province and include an analysis of: (i) the municipal financial situation; and (ii) the capacity of the municipalities to deliver the services for which they are responsible. This study will define the minimum acceptable parameters that the municipalities must exhibit to enable them to participate in the proposed program and receive program funding.

- b. Programs to correct municipal weaknesses, as detected in the MSS.

The investment component (US\$268.1 million) will finance: the rehabilitation, expansion and construction of works falling under municipal responsibility such as neighborhood improvement and facilities, sanitation, streets, and urban lighting; studies, plans, evaluations, and supervision of the works to be financed under this component; municipal master tax files in the design and implementation stage; procurement of equipment and machinery needed by the municipalities to deliver the services for which they are responsible, where no other projects exist to finance those necessities.

**ENVIRONMENTAL
CLASSIFICATION:**

The Environmental Committee classified this as a Category III operation at its meeting on November 16, 1992.

BENEFITS:

Municipal strengthening is expected to result in tighter financial discipline, better allocation of resources with greater transparency and clearer focus, and a more rational system for allocating subsidies.

The projects to be financed under the program will provide local services whose purpose is to improve the quality of life of communities. The increase in coverage of such services will chiefly benefit low-income groups. It is estimated that the program will also create jobs in the equivalent of 110,000 person-months.

RISKS:

In the process of State reform, especially with regard to the decentralization of functions to the provincial and particularly to the local governments, the institutional frameworks have experienced changes and are still in transition. Provincial and municipal legislation must be made to reflect these changes. Should this not be done in a timely fashion, the benefits of the program which derive from the systematization of fiscal relations between the provincial and municipal governments could be affected. To minimize this risk, the program envisages that the Bank and the national coordinating unit will convince the provinces to adopt suitable municipal tax sharing systems. At the annual review meetings the Bank will assess the headway made in this area.

Institutional and operational weaknesses, compounded by shortcomings in staffing structure and numbers, stand in the way of good administration and management of local services. The MSS and the institutional development program must pay special attention to these aspects in order to minimize risks.

Political favoritism by provincial governments could possibly restrict the program's benefits to certain municipalities. To avoid this risk, the program makes the national coordinating unit responsible for hearing appeals brought by the municipalities regarding decisions made by the provincial executing units on the eligibility of municipalities and projects.

THE BANK'S
COUNTRY AND
SECTOR STRATEGY:

The country strategy includes support for programs linked to the decentralization of services to the provincial and municipal levels, particularly investment projects to strengthen the administrative, technical, and financial capacity of provinces and municipalities so that they will be able to shoulder the responsibilities of delivering the services transferred from the federal government. This program is consistent with the strategy.

SPECIAL
CONTRACTUAL
CONDITIONS:

Conditions precedent to the first disbursement:

(i) passage of at least one provincial act which permits the municipalities in that province to participate in the program; (ii) implementation of the program's Operating Regulations; (iii) signature of at least one agreement for the transfer of funding from the borrower to one of the participating provinces; and (iv) establishment of the program's executing unit.

Other contractual clauses:

The Bank's loan contracts will contain stipulations regarding: (i) the performance of a study establishing parameters for measuring the progress made by the municipalities (paragraph 2.6 of the loan proposal); (ii) program follow up (paragraphs 3.33 and 3.34); (iii) cost recognition (paragraph 3.38); (iv) cost recovery (paragraphs 3.27 and 3.28); (v) use of funds recovered (paragraph 3.48); and (vi) auditing (paragraph 3.49).

I. FRAME OF REFERENCE

A. The country

1. Institutional framework

- 1.1 The Argentinian constitution states that the country is to be organized as a federation, and that each province is to have its own provincial constitution establishing the type of municipal system that will apply within its territory. It also establishes that each provincial constitution is to provide for municipal autonomy, regulating municipal jurisdiction and powers in the institutional, political, administrative, economic, and financial areas. Thus, the federal constitution makes the provinces responsible for the municipal system.
- 1.2 Argentina has three levels of government: federal, provincial, and municipal. It has 23 provinces and 1,717 local governments, of which 1,029 are full-fledged municipal governments. The Municipality of the City of Buenos Aires, which has a special system of government that is provincial in nature, should be added.

2. Economic framework

- 1.3 In the 1980s the Argentinian economy was marked by instability and stagnation, chiefly due to the high fiscal and quasi fiscal deficits. In consequence, by 1989 inflation was 4,923% and real per capita income fell by 2.2% during that decade. Investment, which had been 25% in 1980, fell to 14% of GDP by 1990.
- 1.4 This situation forced the current government to adopt an economic reform program aimed at achieving stability and sustained growth, which was coupled with a redefinition of the role of the State on the federal, provincial, and municipal levels, in order to boost the overall efficiency of public sector management.
- 1.5 Inflationary expectations were checked in 1991 as a result of the convertability plan and tight fiscal policy which led to a strong influx of capital and remonetization of the economy. The result was a sharp jump in monetary investment, mirrored real GDP growth of 26% between 1990 and 1993. The economic program was accompanied by adjustment and fiscal reform policies, privatization, decentralization, and the deregulation of economic activity. The strategy includes the adoption of measures in the three areas discussed below.

a. Fiscal reform

- 1.6 A fiscal reform process has been launched to reestablish the tax base which had been severely eroded, contributing to the pressure on the fiscal deficit. The growth in fiscal income resulting from

the reform boosted revenues, not including social insurance, from 8.7% of GDP in 1990 to 11.4% in 1993. This led to an increase in the primary fiscal surplus, excluding privatizations, from 1% of GDP in 1990 to 2% in 1993, and complied with the targets of the Extended Fund Facility of the International Monetary Fund. To consolidate the fiscal gains, two pacts were agreed upon with the provinces, one in 1992 and one in 1993, to induce fiscal reforms on the provincial and municipal levels.

b. Decentralization

- 1.7 The transfer of activities from the federal to the provincial governments and, consequently, to the municipalities, forms part of the country's political and administrative decentralization strategy. The municipalities are acquiring greater relevance within the public apparatus. Since 1983, the main cities have tended to step up their regulatory functions and their tax collecting capacity. This can be most clearly seen in the provinces that have established new constitutions since 1986, such as Río Negro and Salta, and in the terms of the federal pact of August 1993.
- 1.8 Despite these efforts, public social spending for which the municipalities are responsible grew during the period 1980-1992 only from 0.97% to 1.18% of GDP. In contrast, the provincial share (including the Municipality of Buenos Aires) in public social spending rose from 5% of GDP to about 7% over the same period, mainly owing to higher spending on education and culture, social security, and health care. In other words, while provincial social spending grew by 40%, municipal spending grew by just 22%.
- 1.9 The slower headway being made sharing responsibilities with the municipalities is due to the fact that municipal functions and the funding required to carry them out are still being established.
- 1.10 In order to move ahead with the decentralization of services, changes must be made in fiscal relations between the provincial and municipal governments. However difficulties have been encountered owing to the fact that the provisions governing municipal functions and resources are contained in 23 provincial constitutions that differ in their approaches and in the extent to which they have established such provisions.

c. Privatization

- 1.11 Among the main causes of the fiscal deficit were the losses systematically posted by public enterprises which had to be covered out of federal government transfers. In the 1980s these losses averaged about 6% of GDP.
- 1.12 This situation and the need to redefine the role of the State led the federal government to adopt an extensive public-enterprise

privatization program as one of the key tools in its policy to rationalize the State and balance public finances. The aim is to drive down the fiscal deficit by eliminating such transfers, in addition to handing over to the private sector those activities in which it is more efficient.

- 1.13 On the municipal level, the privatization process presents a broad array of possibilities owing to the nature of the services municipalities are called upon to provide the community. The possibilities range from small companies engaged in trash collection, to medium-sized and large companies that manage potable water services. Although services of this kind have already been privatized in Buenos Aires and other large municipalities, privatization in smaller towns will have to wait for the future.

B. The provinces

1. Process of decentralization, tax sharing, and constitutional reform

- 1.14 The new national tax sharing act with the provinces was promulgated in 1988 giving them 58% of all taxes, except for those on foreign trade. Under this income redistribution, the provinces were given greater responsibility for decision-making and government administrative functions. The process also led to changes in the legal-institutional order involving a recognition, through national legislation, of the need to grant the municipalities greater autonomy and to highlight their role in the community.
- 1.15 As part of the decentralization process, the provincial governments were given greater responsibility for hospital management, secondary education and part of vocational education, starting in 1993, which is an extension of the process initiated in 1976 with the transfer of primary education, sanitary works, and some hospitals to this level of government.
- 1.16 To support the decentralization and fund-sharing process, the federal and provincial governments signed two agreements that establish additional parameters for the federal system. Under the fiscal pact of August 1992, the federal government guarantees the provinces a minimum monthly income out of the funds eligible for sharing, allocates part of those funds to financing the social security debt, and decentralizes the control of specific funds, such as the housing fund (FONAVI). Under the second federal pact of August 1993, the federal government undertakes to increase the monthly minimum income and takes over the social security deficit in exchange for substantial reforms in provincial administration. The reforms focus on efforts to reduce domestic production costs through a reduction in taxes on productive activities (even income tax), and provincial deregulation and privatization.

- 1.17 The new national constitution was proclaimed in August 1994, and contains a provision whereby all direct and indirect taxes - except for those that are specifically earmarked - are to be shared with the provinces.
- 1.18 The sharing arrangements will be set out in legislation drawn up on the basis of agreements between the federal and provincial governments, and passed by absolute majority of each chamber of congress, guaranteeing that the funds will be transferred automatically. The distribution of resources between the federal government and the provinces and the Municipality of Buenos Aires will be directly linked to the powers, services, and functions of each, with priority given to equitable development.
- 1.19 Other important changes of relevance are: special funds will be established or modified by an absolute majority of congress; the provinces may create economic and social development regions, and may enter into international agreements, with the knowledge of the federal congress, provided they are not incompatible with the nation's foreign policy and do not affect its public credit.
- 1.20 The adjustments being made in the provinces will also involve the transfer of new responsibilities and powers to the municipalities, which must therefore develop adequate institutional capacity.

2. Provincial and municipal relations

- 1.21 The Argentinian political system is provincially based. When the provinces created the federal government they delegated to it the main functions of the State reserving for themselves those they would execute directly or which they would delegate to their municipalities, which form the third level of government. The municipalities were empowered to autonomously carry out all the activities delegated to them. The province was to stipulate the framework in which such activities were to be carried out and to monitor the process.
- 1.22 In this context, the provinces drew up their own constitutions, including the basic features of their municipal systems. However, for the large part, the financial frameworks that would make it possible for the municipalities to fully exercise their autonomy are not completely in place, and therefore the municipalities continue to rely heavily on discretionary allocations.
- 1.23 Discretionary allocations continue to play a large role even in provinces that have established greater financial independence, simply because the system whereby resources are allocated permits discretionality. The systems do not include the principle of universality and equality of opportunity in their eligibility

criteria, and so decisions are made on a case-by-case basis, which makes for undesirable biases.

C. The municipalities

1. Institutional aspects

- 1.24 Although the municipalities are the level of government that is closest to the community, they have not participated fully in the decentralization process. Their funds come mainly from provincial government transfers. The sources of the revenues they collect directly are generally taxes on services or payments for service concessions. The limited fiscal authority of the municipalities and their scant ability to mobilize resources and recover the costs of the services provided are mirrored in their dependence on tax sharing.
- 1.25 To prepare the program, the Department of the Secretary of Social Development, through its Secretaría de Vivienda [Office of the Under Secretary of Housing] (SSV), prepared a study on municipal autonomy and jurisdiction. The study notes that the municipalities enjoy different degrees of autonomy and authority depending on the province to which they belong, and are empowered to regulate, execute works, and provide services in those aspects that are most closely linked to the local context. They are not authorized to pass laws, and their legislation, which is only valid within their city limits, takes the form of municipal ordinances which are always subordinate to national and provincial legislation.
- 1.26 Therefore, even though a municipal system exists on paper, marked by a reasonable degree of independence from the other levels of government, the municipalities have no incentives to mobilize resources or to borrow, and lack appropriate mechanisms to enable them to effectively deliver the services they are called upon to provide.

2. Municipal sphere of action

- 1.27 The study mentioned in paragraph 1.25 examined a statistically representative sample of 109 municipalities, and established that municipal authority extends to those services and local works which are divisible and which can be provided locally as measured by criteria for technical, economic, and financial efficiency. The public services lying in the municipal sphere are:
- a. collection and treatment of solid waste;
 - b. city streets;
 - c. markets;
 - d. parks and green spaces;
 - e. cemeteries;
 - f. potable water;
 - g. sewers;

- h. storm sewers;
- i. protection against erosion and flooding;
- j. public lighting;
- k. community facilities (neighborhood centers, kindergartens, primary health care posts);
- l. local transport and bus terminals;
- m. education up to the end of secondary school, in cooperation with the provincial government;
- n. policing power in environmental matters, whose extent varies from province to province.

1.28 The first five items listed are municipal responsibilities in over 90% of the cases studied. The rest of the items were municipal responsibilities in over 50%. Although fewer in number, some municipalities are also responsible for potable water and sewer services, flood protection, and primary health care.

1.29 The study also showed that some provinces plan to transfer other services, which are currently being provided by the provincial governments, to the municipalities, such as primary education and further decentralization of primary health care.

3. Finances and municipal tax sharing

1.30 In preparing the program, the Department of the Secretary of Social Development, through the SSV, prepared a study on municipal tax sharing systems in the Argentine Republic. This study analyzed the different provincial tax sharing systems, sharing formulae in 13 representative provinces, an econometric study of municipal finances in three provinces, and a study on decentralization. It produced the following results:

- a. All of the provinces have a tax sharing system, except for La Rioja which has suspended implementation of the respective legislation.
- b. Fiscal transfers from the provinces to the municipalities are automatic (shared) and discretionary (unsystematic).
- c. Tax sharing complies with the first principle of adequacy, in other words per capita transfers have remained constant in real terms. It has not complied with the second principle of adequacy, i.e. the sums transferred, combined with a reasonable fiscal effort by the municipalities, have not been sufficient to enable them to maintain satisfactory service levels. Therefore, it has been necessary to either increase discretionary transfers or reduce the quality of service. Although provincial government transfers rose from 42.1% of municipal resources in 1980 to 70.7% in 1988, this has not been sufficient to provide acceptable quality and coverage.

- d. The econometric analysis points to the existence of a "substitution effect" between own resources and transfers which indicates that despite the fact that most of the formulas used for dividing up the resources include incentives for fiscal effort, they do not weigh as heavily as they should.
- e. Allocations are predominantly redistributive, and per capita transfers to smaller, less-developed municipalities with the weakest fiscal potential tend to be higher.
- f. Sharing formulae are extremely varied and all proposals for a new system of transfers to improve on the existing system must take account of the individual characteristics of each province.

4. Deficit in services on the municipal level

- 1.31 Potable water coverage at 67% and sewer service at 39% are insufficient. Furthermore, problems with flooding and the lack of storm sewers can be serious in the cities, as can the lack of municipal facilities (daycare, homes for the elderly, and so on). Many city streets are unpaved, and the lack of bus terminals and rising maintenance costs pose problems for the municipalities.
- 1.32 According to the study mentioned in paragraph 1.30, almost all the municipalities (94.6%) suffer from some kind of shortfall in services. The lack of sewer systems or their poor quality is a problem in 44% of municipalities. Thirty-seven percent of the municipalities suffer from serious flooding caused by overflowing rivers or lakes.
- 1.33 The next problems in declining order of frequency (between 37% and 24%) involve the lack of infrastructure and/or urban facilities, such as, pavement, storm sewers, and infrastructure in general.
- 1.34 Using the sample of municipalities and expanding the results to the entire universe, it has been estimated that investment requirements in services and facilities for all the country's municipalities run to US\$8.5 billion.

D. Sector financing

1. Bank participation in the sector

- 1.35 The Bank has extended five loans totalling the equivalent of US\$171.2 million for the urban sector in Argentina, one of which was approved in 1962, two in 1966, and two in 1987.

a. Comprehensive urban development program

- 1.36 Loans 206/IC-AR and 514/OC-AR totalling US\$122 million, approved in 1987, represent the Bank's contribution to the financing and

implementation of the program, whose total cost was estimated as US\$300 million. The objective is to improve access to services and the quality of life by building works involving urban infrastructure and facilities, including the corresponding technical assistance projects, in 23 of the 24 provinces. The executing agency is the Subsecretaría de Vivienda [Office of the Under Secretary of Housing] (SSV) whose executing unit, tapping the experience gained in that program, has also been responsible for preparing the background information for the project presented in this document.

1.37 The Bank's loan was committed within the original contractual term, despite the fact that the start of execution took place in one of the most difficult periods for the Argentinian economy.

1.38 As of July 30, 1994, 100% of loan 206/IC-AR in the amount of US\$120 million had been disbursed, as had 84% of loan 514/OC-AR, for US\$1.5 million.

b. Financial recovery and economic development program for the Argentine provinces

1.39 Through loan 619/OC-AR in the amount of US\$200 million (with cofinancing in the same amount from the IBRD), the Bank is supporting the program in question whose total cost is US\$575 million. Bank financing is restricted to the provincial sphere of action, and therefore is complementary to the program proposed here. The provincial program was declared eligible for disbursement in November 1991, and consists of two subprograms:

- a. An institutional development subprogram intended to strengthen the provinces and to prepare investment studies and projects aimed at making them financially self sufficient; and
- b. A subprogram to finance investments in basic services falling under provincial jurisdiction, in order to repair, maintain, rehabilitate, and expand public services, including cost recovery to lessen reliance on provincial budgets.

1.40 During the initial execution stage, in accordance with the short-term objectives, the program focused its activities largely on promoting the institutional development component, and subsequently began to promote the investment component.

1.41 To date, all the provinces with the exception of Santa Cruz have been declared eligible for the program. Since the Bank and the executing unit agreed on project-evaluation methodologies in 1993, the executing unit has approved provincial projects accounting for 72.3% of the loan. However, disbursements totaled just 4.1% as of August 31, 1994, and the effective real level of commitment (signed contracts) was 7.6% although the figure should rise to 35% by the end of 1994.

c. Other related programs

- 1.42 The Bank has also funded the construction of potable water systems in rural and urban areas through 13 loans in the equivalent of US\$445 million. In September 1991 it approved two loans for US\$165 million for the institutional, financial, and operational strengthening of provincial electricity companies. Operations for reforms to and investments in the primary education sector and for rural potable water services are in the pipeline and are expected to be approved in 1994. Operations for provincial agricultural development and provincial productive infrastructure are planned for 1995.

2. Activities of other lending agencies in the sector

- 1.43 The IBRD's municipal development program is in the final stage of execution, and is limited to financing works with a ceiling of US\$1.5 million per project, in the provinces of Buenos Aires, Santa Fe, Córdoba, La Pampa, and Neuquén.
- 1.44 In the second half of the 1980s, it extended three loans totalling US\$330 million, two of which were for potable water (US\$160 million) and the third for flood rehabilitation (US\$170 million).

E. Bank strategy in the sector

- 1.45 The country strategy includes support for programs to decentralize services on the provincial and municipal levels, particularly investment projects to strengthen the administrative, technical, and financial capacity of the provinces and municipalities to enable them to provide the services transferred by the federal government.

II. THE PROGRAM

A. Program objectives

- 2.1 The general objective of the program is to support the municipalities in their actions to improve the quality of life of their inhabitants, particularly those belonging to low-income groups, and the federal government in its policy to decentralize public finances and place them on a sound footing.
- 2.2 To attain these objectives, the program will support:
 - a. The rehabilitation, expansion, and construction of works for which the municipalities are responsible;
 - b. Strengthening for the municipalities in institutional, financial, and technical aspects in order to improve the efficiency and coverage of the services they already provide, and ready them to take over other services that will be transferred to them by the provinces;
 - c. Greater citizen participation in determining local investment priorities;
 - d. Actions to make the system for allocating funding to the municipalities transparent and universally accessible; and
 - e. Assistance for the municipalities in improving their fiscal efficiency through adequate tax sharing systems, cost recovery, and cost rationalization.

B. Description

- 2.3 At the request of the Argentinian authorities, this program has been designed in tandem with a parallel operation by the IBRD that is substantially similar in nature. Consequently, it was decided that ten of the provinces would be eligible to participate in the Bank's program, another ten would be eligible for the IBRD program, and four could participate in both programs. The provinces only eligible for the IDB program will be: Río Negro, Entre Ríos, Tucumán, San Luis, Jujuy, San Juan, Chubut, Salta, Chaco, and Santiago del Estero. The provinces that will be able to participate in both programs are: Córdoba, Santa Fe, Buenos Aires, and Mendoza. In this case, the Bank's program will finance projects costing more than US\$2 million, and the IBRD will finance those costing less.
- 2.4 The provinces were divided up between the two Banks based on the IDB's wish to finance the less-developed provinces, to continue its work in the company of the IBRD in provinces in which it has

already been active, and to maximize the financing for projects in the representative sample prepared with IDB funding and assistance.

- 2.5 The program will include an institutional development component and an investment component.

1. Institutional development

- 2.6 The institutional development component (US\$20 million) will be composed of two closely-related subcomponents:

a. A municipal situation study (MSS) to be conducted in accordance with the terms of reference agreed upon with the Bank in each province, including an analysis of: (i) the municipal financial situation; and (ii) the capacity of the municipalities to deliver the services they are responsible for providing. The study will define the minimum acceptable parameters that the municipalities must meet to be able to participate in and receive funds from the proposed program.

b. Programs to correct shortcomings based on the findings of the MSS.

- 2.7 In its analysis of the financial situation, the MSS will study the financial relations between the provinces and their municipalities, the structure of the municipal tax sharing system, the size of discretionary transfers, and the importance of the municipalities' own resources, *inter alia*.

- 2.8 In its study of the capacity of the municipalities to deliver services, the MSS will look at: (i) the organizational structure; (ii) the human resource profile; and (iii) the capacity of the municipalities to provide services and to cope with the increase in services that will accompany the decentralization process.

- 2.9 The studies will be used to establish parameters in the following areas: (i) resources; (ii) costs; (iii) organizational structure; (iv) human resources; and (v) the provision of municipal services. Based on the result of the MSS, the national coordinating unit will encourage the provinces to rework their municipal tax sharing systems.

- 2.10 This component will also finance:

a. Program operations, including the consulting services required by the national coordinating unit and the provincial executing units for their activities; and

b. Contracts for financial auditing and program management services.

2. Investments

- 2.11 The investment component (US\$268.1 million) will finance studies, designs, evaluations, and supervision of works; municipal master tax files in the design and implementation stage, including the equipment necessary to operate them; the procurement of equipment and machinery for the provision of municipal services provided no other projects to finance it exist; and the rehabilitation, expansion, and construction of municipal works in the sectors listed below, although other sectors may be included once the Bank and the Department of the Secretary of Social Development agree on the pertinent methodologies:

i. Urban facilities

- a. Community centers and child-care facilities
- b. Bus terminals
- c. Parks, green areas, and playgrounds

ii. Urban sanitation

- d. Protection against erosion and flooding
- e. Storm sewers
- f. Trash collection and disposal

iii. City streets

iv. Urban lighting

v. Neighborhood improvements

- 2.12 Although the municipalities are responsible for more activities than the five listed in the preceding paragraph, only activities that have not received Bank financing and activities for which projects have been identified which comply with the program's eligibility criteria were considered.

C. Size of program

- 2.13 The following factors were taken into account when scaling the program:

- a. The urban infrastructure deficit: the results of a survey of the 109 municipalities in the sample were expanded to the entire country, pointing to a deficit as of May 1993 of close to US\$8.5 billion. This figure covers only works for which projects have been developed to some degree, ranging from the idea stage to the final design, and therefore the true short-fall is much higher. Accordingly, this program plus the program to be funded by the IBRD will only address a fraction of the total requirements.

- b. The institutional-strengthening requirements of the municipalities: diagnoses were carried out to scale this component, and the institution-building activities required by ten different municipalities were defined. The average unit cost was US\$40,000, which expanded to all the municipalities in the provinces participating in the program amounts to US\$19.7 million.
- c. Local counterpart: in determining the makeup and size of the local counterpart, the financial capacity of the municipalities was taken into account in order to minimize federal contributions.
- d. The execution capacity of the Secretaría de Desarrollo Social [Department of the Secretary of Social Development] (SDS) and the municipalities: for the purposes of the program sample, the SDS and the municipalities were able to carry out 34 projects worth close to US\$105 million, and therefore problems are not anticipated in identifying or preparing projects for the program.

D. Cost of the program and financing plan

1. Total cost

- 2.14 The program is estimated to cost the equivalent of US\$300 million, as per the following table:

TABLE II-1
TOTAL COST AND SOURCES OF FINANCING
(US\$ millions)

		IDB			LOCAL COUNTERPART					
					Municipality	Federal government		Total	Total	%
		OC	FSO	Total		MIS*	IDS*			
		Foreign exchange	local currency							
1.	Investments	170.7	29.7	200.4	26.8	40.9	—	67.7	268.1	89.3
2.	Institutional development	6.0	—	6.0	—	—	14.0	14.0	20.0	6.7
2.1	Municipal situation study	0.3	—	0.3	—	—	1.5	1.5	1.8	0.6
2.2	Program to correct shortcomings	5.7	—	5.7	—	—	12.5	12.5	18.2	6.1
3.	Program operation	—	—	—	—	—	8.3	8.3	8.3	2.7
3.1	Executing unit	—	—	—	—	—	5.0	5.0	5.0	1.7
3.2	Contracts with consultants, project evaluation	—	—	—	—	—	2.3	2.3	2.3	0.7
3.3	Auditing						1.0	1.0	1.0	0.3
4.	Inspection and supervision	1.8	0.3	2.1	—	—	—	—	2.1	0.8
5.	Recoveries, PFF	1.5	—	1.5	—	—	—	—	1.5	0.5
TOTAL		180.0	30.0	210.0	26.8	40.9	22.3	90.0	300.0	100.0
%		60.0	10.0	70.0	8.9	13.7	7.4	30.0	100.0	

*MIS=Municipal investment subaccount; *IDS=Institutional development subaccount

2. IDB financing

a. Sources

2.15 The funding will consist of: (a) a loan for US\$180 million in foreign exchange from the ordinary capital (60% of the total cost) 1/ and (b) a loan for US\$30 million in local currency from the FSO.

1/ According to document AB-1683, the matrix for A countries allows for financing in foreign exchange of up to 50% of the total cost plus an additional 10% if most of the program's beneficiaries belong to low-income groups.

b. Terms and conditions

2.16 The following conditions are proposed for the loans:

Amortization period:	25 years
Commitment period:	4 years
Disbursement period:	6 years
Grace period:	6.5 years
Interest rate:	variable (OC) 4% (FSO)
Inspection and supervision:	1% of the loan
Credit fee:	0.75% of the undisbursed balance (OC)

3. Local contribution

2.17 The local contribution, in the equivalent of US\$90 million, will come from the municipalities (US\$26.8 million or 8.9% of the total cost) and the federal government (US\$63.2 million or 41% of the total cost). The analysis of the financial situation of the municipalities indicates that they should not encounter problems in making their share available on time.

4. PPF recovery

2.18 Resources from the first disbursement will be used to totally repay loan PPF 761/OC-AR in the amount of US\$1.5 million which was used to prepare the information required to analyze the proposed operation.

III. PROGRAM EXECUTION

A. Execution mechanisms

- 3.1 The government has made the Department of the Secretary of Social Development responsible for coordinating and supervising program execution.
- 3.2 The department will execute the program through the Office of the Under Secretary of Housing (SSV), where the national coordinating unit is located. The unit is successfully performing similar work for the urban development program and has also prepared the program under consideration here. It will set up two subaccounts for this program: (i) institutional development subaccount; and (ii) municipal investment subaccount.
- 3.3 In order to decentralize program execution, and considering that one of the basic functions of the provinces is general planning within the provincial jurisdiction and supervision of the actions of the municipalities within their boundaries, the provinces will participate in the program by passing a "borrowing act".
- 3.4 Under this provincial legislation, the provincial executive branch will be authorized to borrow from the federal government, accepting the program's conditions and those of the loan contacts between the federal government and the IDB, and agreeing to allocate the province's share to the municipalities. Approval of at least one borrowing act will be a prior condition to the first disbursement of the loan.
- 3.5 Provincial executing units will be set up which may, depending on the preference of each province, be the same ones that are executing the financial recovery and economic development program for the Argentine provinces, or be new units to be set up as demand warrants. The provincial executing units will be responsible for promoting the program, executing the municipal institutional development component, providing guidance for the municipalities, and approving projects within the discretionary limits described below.
- 3.6 Execution will be carried out in accordance with the operating and financial procedures established in: (i) the stipulations contained in the loan contract between the Bank and the borrower; (ii) the program's Operating Regulation; (iii) the program execution manual which forms an integral part of the Operating Regulations; and (iv) the subsidiary loan contracts between the SDS and the provinces.
- 3.7 Signature of at least one loan contract between the SDS and a province and implementation of the program Operating Regulations

will be conditions precedent to the first disbursement of the financing.

1. Execution cycles for the institutional development component

3.8 The component will be carried out in three cycles with clearly-identified actions that are summarized in Figures III-1 to III-3. The numbers in parenthesis indicate the sequential steps in each cycle:

- a. Cycle for municipal diagnosis and the program to correct weaknesses (Figure III-1): (1) the municipality asks the provincial executing unit to conduct a municipal diagnosis; (2) this diagnosis is carried out jointly by the municipality and the unit, with support from consultants; (3) it will produce guidelines for the program to correct weaknesses, including a definition of the stages and their respective administrative and financial targets; and (4) the municipality is given the program to correct weaknesses.
- b. Financing cycle (Figure III-2): (1) the municipality obtains from the institutional development subaccount the financing it requires to (2) hire the consulting services to (3) implement the program to correct weaknesses. The provincial executing unit will provide the financing once an institutional development contract has been signed.
- c. Execution and cost recovery cycle (Figure III-3): (1) the municipality implements the program to correct weaknesses and (2) as a result its current savings will increase; (3) the increase in municipal resources is used to (4) repay the loan received from the institutional development subaccount and (5) the remaining resources, once fiscal balance has been attained, can be put into the investment component.

FIGURE III - 1

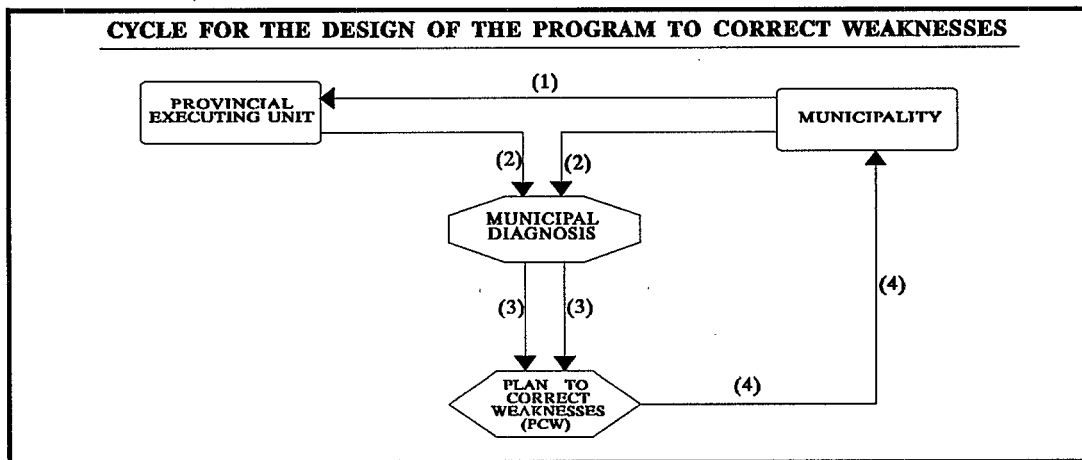


FIGURE III - 2

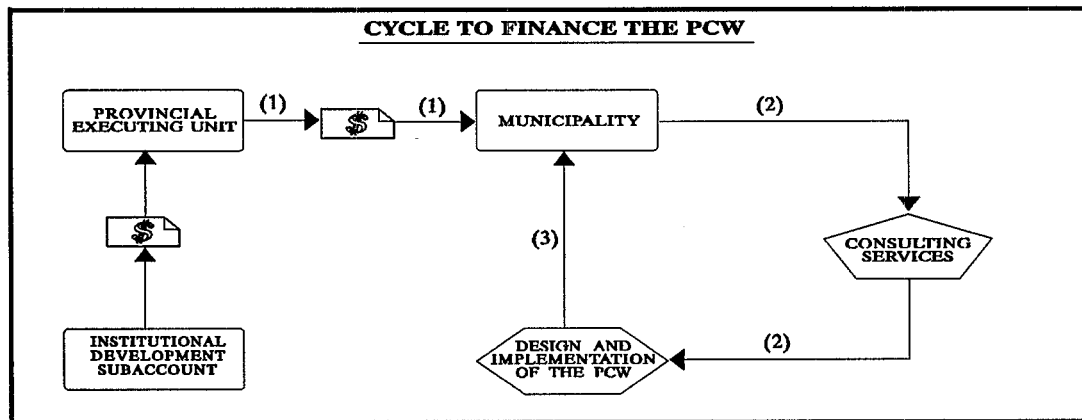
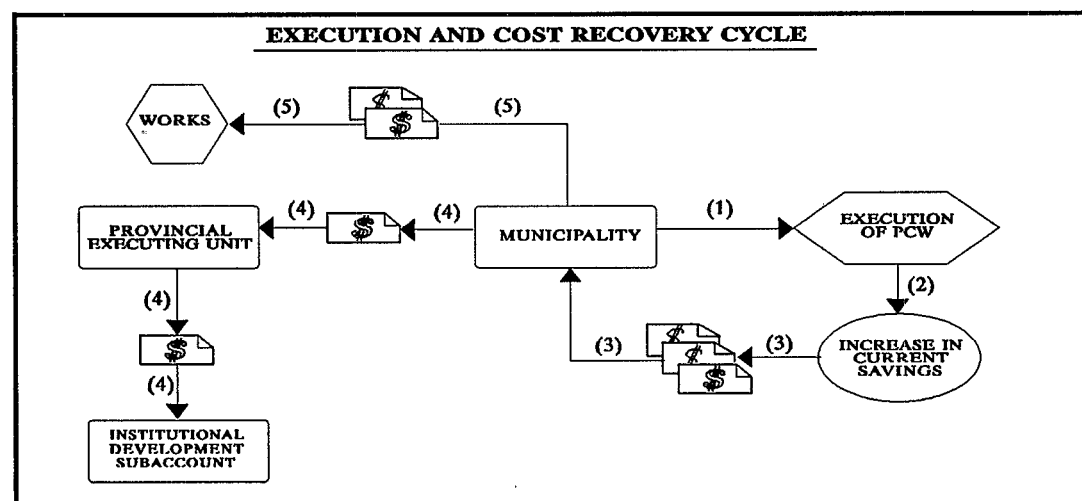


FIGURE III - 3



2. Cycles for executing the works component

3.9 This component will be executed in three cycles with clearly-identified actions that are summarized in Figures III-4 to III-6. The numbers in parenthesis indicate the sequential steps in each cycle:

- a. **Project eligibility and design cycle (Figure III-4):** (1) the municipality identifies a need and prepares a proposal to address it which it presents to the provincial executing unit; (2) the executing unit studies it and if it finds that the proposal complies in principle with the eligibility criteria mentioned below, it will give its approval; (3) the municipality works the proposal up into a project in final form, including all necessary evaluations.
- b. **Project financing cycle (Figure III-5):** (1) the municipality presents the final project to the provincial executing unit for financing, including whatever evaluations are necessary; the unit revises it and verifies that it complies with all the program eligibility criteria; (2) if it does, the unit will lend funds for it from the municipal investment subaccount.
- c. **Execution and cost recovery cycle (Figure III-6):** (1) the municipality calls for tenders for the works, in accordance with the program procedures; (2) the municipality studies the bids, and in accordance with the program procedures awards the contract; (3) the contractor carries out the work and (4) through the municipality it is delivered to the beneficiaries; (5) the municipality using the appropriate cost recovery mechanism, charges the beneficiaries for the work; (6) the municipality uses these resources to repay the provincial executing unit for the loan; (7) the unit uses these resources to repay the national coordinating unit.

FIGURE III - 4

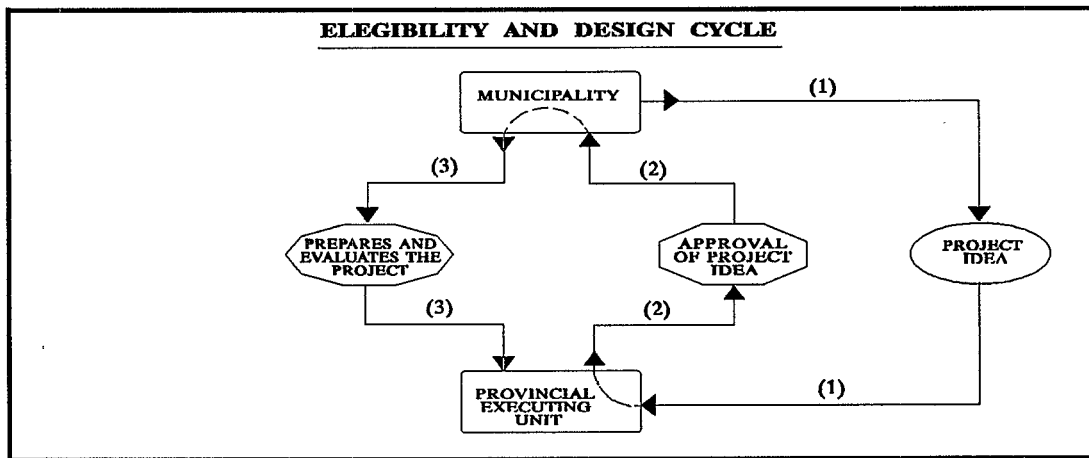


FIGURE III - 5

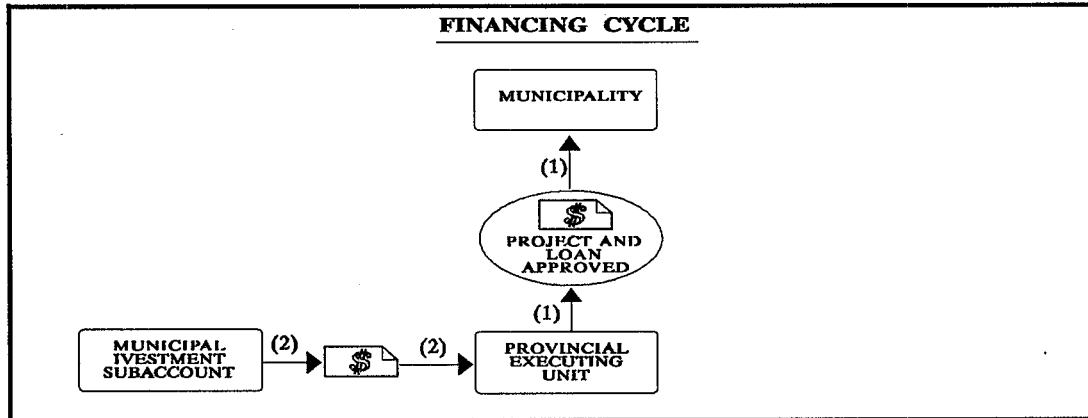
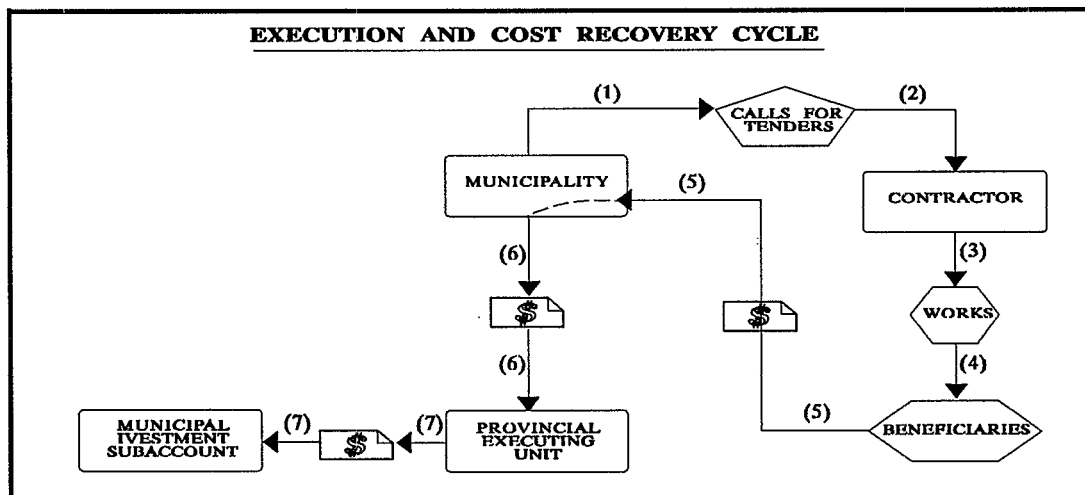


FIGURE III - 6



B. Mechanism for the transfer of funds

- 3.10 To formalize the transfer of funding from the Bank loan and the local contribution, the government will set up an institutional development subaccount and a municipal investment subaccount, to be administered and operated by the Department of the Secretary of Social Development.
- 3.11 The program funds earmarked for the department will be transferred by the government to finance: (i) the study on the municipal situation to be conducted in each province; (ii) the program to correct weaknesses, as detected in the situation study; (iii) program operations; and (iv) the contracting of services for accounting and financial audits and program management.
- 3.12 The program funding earmarked for the municipal investment sub-account will be transferred by the government to finance works, equipment, studies, and designs in sectors previously agreed upon with the Bank.

C. Operating Regulations

- 3.13 Program execution will be governed by the Operating Regulations which can be consulted in REL/SO1. They include the mechanism for allocating quotas to the provinces, the program's operating mechanism, and the eligibility criteria for municipalities, sectors, and projects. The following documents, which define the rules for the operational aspects of program execution, will form an integral part of the regulations:
- a. Program execution manual
 - b. Model for the borrowing act
 - c. Model for the institutional contract
 - d. Model for the municipal investment contract
 - e. Model bid documents
 - f. Contracts for works and services
 - g. Accounting plan
- 3.14 The main parts of the Operating Regulations include:
- 1. Allocation of program funds
- 3.15 Initially, program funds will be allocated to the provinces through the establishment of quotas. The government will allocate all the resources in keeping with the following criteria:
- a. 50% of the funds will be allocated using the secondary weighted distribution coefficients contained in Act 23.548 on federal tax sharing; and
 - b. 50% will be allocated using the unmet weighted basic needs index as it appears in the poverty map for Argentina drawn up

by the Economic Programming Department of the Argentinian Ministry of the Economy.

- 3.16 The initial allocation for the provinces of Buenos Aires, Córdoba, Mendoza, and Santa Fe, which will also participate in a similar operation with the IBRD, will be established by taking 50% of the amount obtained from applying the criteria set out in paragraph 3.15.
- 3.17 The funds not assigned under the preceding paragraph will be made available to provinces that have committed 100% of their initial quotas and whose municipalities have committed 75% of those funds. A provincial commitment will be defined as the signature of an institutional development contract or a municipal investment contract with a municipality, and a municipal commitment will be defined as the signature of contracts for works or services, or the procurement of goods.
- 3.18 If the initial funds earmarked for the provinces have not been committed within two years after the program begins, the uncommitted balance will be cancelled and the sums will be added to the unallocated funds mentioned in the preceding paragraph.

2. Discretionary limits

- 3.19 Once the provincial executing unit has completed its analysis of all aspects of the institutional, technical, environmental, financial, economic, and legal eligibility of each request for financing, it may approve the loan without the need for prior authorization from the national coordinating unit or the Bank in the event that the total for each individual project is not over US\$1.5 million.
- 3.20 If a project costs more than that figure but not over US\$5 million, the provincial executing unit will submit it to the national coordinating unit. If the project costs more than US\$5 million, the national coordinating unit will submit it to the Bank for review and approval.
- 3.21 These limits will be revised during the annual program evaluation.

3. Eligibility criteria

i. For provinces

- 3.22 Initially, the provinces that will participate in the program are Río Negro, Entre Ríos, Tucumán, San Luís, Jujuy, San Juan, Chubut, Salta, Chaco, Santiago del Estero, Córdoba, Santa Fe, Buenos Aires, and Mendoza.
- 3.23 To be eligible for program financing the provinces must:

- a. have enacted the borrowing act; and
- b. be eligible for the provincial financial recovery and economic development program.

ii. For the municipalities

3.24 All municipalities will be eligible for the institutional development component.

3.25 To be eligible for the investment component the municipalities must:

- a. have a ratio between current income and spending of 1.0 or over, both expressed on the same base, cash, or amounts due. In calculating this ratio, shared revenues are considered income but not unsystematic or discretionary transfers;
- b. demonstrate that the entire debt service (including installments and interest) is not more than 15% of total income (net of discretionary transfers and borrowings) for the preceding year, adjusted by inflation;
- c. comply with the clauses of the institutional development and municipal investment contracts signed under the program.

iii. For sectors and types of projects

3.26 The technical, economic, and financial eligibility criteria for projects to be financed are presented in Table III-1.

TABLE III-1: ELIGIBILITY CRITERIA FOR PROJECTS

TYPE OF WORK	TECHNICAL CRITERIA	ECONOMIC CRITERIA	FINANCIAL CRITERIA
<ul style="list-style-type: none"> - Community centers - Kindergartens and mother and child care facilities 	<ul style="list-style-type: none"> - Analysis of alternative locations. - Availability of services. - Availability of equipment and trained personnel. 	<ul style="list-style-type: none"> - Minimum cost solution. - Study of demand and use of spaces. - Determination of the income level of beneficiaries. - Distributional impact coefficient (DIC) $\geq 80\%$. 	<ul style="list-style-type: none"> - Cost recovery through charges to beneficiaries and from general revenues. The respective percentages must be determined and justified in each case.
<ul style="list-style-type: none"> - Bus terminals 	<ul style="list-style-type: none"> - Frequency study. - Analysis of alternative locations. - Availability of services. - Traffic study. 	<ul style="list-style-type: none"> - Economic analysis of alternatives and cost-benefit with $IRER \geq 12\%$. 	<ul style="list-style-type: none"> - Cost recovery through charges to beneficiaries.
<ul style="list-style-type: none"> - Green areas and recreational areas 	<ul style="list-style-type: none"> - Analysis of alternative locations. - Availability of services. - Availability of equipment and trained personnel. 	<ul style="list-style-type: none"> - Study of demand and use - Economic analysis of alternatives and cost-benefit with $IRER \geq 12\%$. 	<ul style="list-style-type: none"> - Cost recovery through charges to beneficiaries and from general revenues. The respective percentages must be determined and justified in each case.
<ul style="list-style-type: none"> - Sports centers 	<ul style="list-style-type: none"> - Analysis of alternative locations. - Traffic study (accessibility). - Planning in accordance with the demand study. 	<ul style="list-style-type: none"> - Study of supply and demand, uses and income levels of the beneficiaries. - Justification of the use of spaces. - Comparison with cost-efficiency indicators. 	<ul style="list-style-type: none"> - Cost recovery through charges to beneficiaries and from general revenues. The respective percentages must be determined and justified in each case.
<ul style="list-style-type: none"> - Protection against flooding and storm sewers. 	<ul style="list-style-type: none"> - Hydrological and soil studies. - Alternatives for designs and materials. - Analysis of recurrence. 	<ul style="list-style-type: none"> - Economic analysis of alternatives and cost-benefit with $IRER \geq 12\%$. 	<ul style="list-style-type: none"> - Cost recovery through charges to beneficiaries and from general revenues. The respective percentages must be determined and justified in each case.
<ul style="list-style-type: none"> - Solid waste 	<ul style="list-style-type: none"> - Comparative study of different treatment solutions. - Analysis of alternative locations. 	<ul style="list-style-type: none"> - Economic analysis of alternatives and cost-benefit with $IRER \geq 12\%$ for collection. - Minimum economic cost solution for final disposal. 	<ul style="list-style-type: none"> - Cost recovery through charges to beneficiaries and from general revenues. The respective percentages must be determined and justified in each case.
<ul style="list-style-type: none"> - Paving 	<ul style="list-style-type: none"> - Existence of potable water and sewer systems. - Traffic study on main streets and priorities for the remainder. - Comparative study of structural designs and types of pavement. 	<ul style="list-style-type: none"> - Economic analysis of alternatives and cost-benefit with $IRER \geq 12\%$. 	<ul style="list-style-type: none"> - Cost recovery through charges to beneficiaries and from general revenues. The respective percentages must be determined and justified in each case.
<ul style="list-style-type: none"> - Lighting 	<ul style="list-style-type: none"> - Availability of reliable sources of energy. - Study of alternatives for electric circuits and types of lighting 	<ul style="list-style-type: none"> - Economic analysis of alternatives and cost-benefit with $IRER \geq 12\%$. 	<ul style="list-style-type: none"> - Cost recovery through charges to beneficiaries.
<ul style="list-style-type: none"> - Neighborhood improvement 	<ul style="list-style-type: none"> - Neighborhoods that require at least 40% improvement. - At least 70% of beneficiaries own their own land. - Maximum service level: <ul style="list-style-type: none"> • permanent pavement only for the access road and minimum solution with curbing for the other roads. • Storm sewers with surface runoff. • Standard minimum lighting. • Kitchen & toilet $\leq 12m^2$. • Multiple-use room $\leq 20m^2$. 	<ul style="list-style-type: none"> - $DIC \geq 80\%$. - Survey of 100% of the beneficiaries to determine the types and priorities of the works to be included in the project. - If subsidies are required, a study must be made of the system to be used, the amount of the subsidy, and the way it will be allocated. 	<ul style="list-style-type: none"> - Cost recovery through charges to beneficiaries. If subsidies are used, they must be direct and be reflected in the municipal budget.

4. Cost-recovery mechanisms

- 3.27 The fees, charges, contributions for improvements, and taxes collected must, as a rule, cover operating, administration, maintenance, and investment costs. In cases in which it is impossible to clearly identify the project beneficiaries or when a breakdown cannot be justified, the general revenues of the municipality will be used as the cost-recovery mechanism. In such cases, it must be demonstrated that the project will not create a deficit in the municipality's current account.
- 3.28 However, when the socioeconomic level of the population requires, the general rule may be made more flexible to enable the municipalities, without creating a deficit in their current account, to subsidize part of the investment costs in function of the ability to pay of the beneficiary families. These subsidies must be explicit and allocated in specific amounts, following the rules established in the program execution manual.

5. Supervision of the works

- 3.29 Supervision of the construction contracts will be the responsibility of the municipalities. They may carry out this activity directly when they have the technical capacity to do so, or otherwise, they may contract it out to individual consultants or a specialized consulting company. In all cases the nonobjection of the provincial executing unit will be required with regard to the proposed procedure. The cost of supervision will be recognized as part of project financing in the event it is contracted out.

6. Terms and conditions for transfers

- 3.30 The government will transfer program funds to the provinces through subsidiary loan contracts under the same conditions as it obtained them, but adding two points to the average interest rate on the Bank loan.
- 3.31 The provinces will transfer the resources to the municipalities for periods that will vary depending on the type of work, but may not exceed its useful life. The interest rates to be charged by the provinces to the municipalities will be at least 1.5 points higher than the interest rate charged to the provinces under the respective subsidiary loan contracts.

D. Environmental aspects

- 3.32 The projects have been divided into three categories depending on the type of environmental impact involved, i.e. during execution, implementation, or operation. Based on these categories and with the support of the Department of Natural Resources and Human Environment, environmental impact studies will be conducted for projects with different levels of complexity. The procedures for

environmental quality control of the program will form part of the program execution manual, which is an integral part of the Operating Regulations.

E. Program follow-up

- 3.33 The borrower, through the executing agency, will submit semiannual reports on program implementation to the Bank, as required in the program execution manual. These reports will be presented to the Bank within the 90 days counting from the close of each calendar semester, during program execution and for an additional year after the final disbursement.
- 3.34 Annually during program execution the Bank and the borrower will perform a joint evaluation in order to examine compliance with program objectives in fiscal aspects (particularly the municipal tax-sharing schemes) and institutional aspects, and the projects financed. The results of the review could lead to the discontinuance of the investment subcomponent. The semiannual progress reports will be used for this purpose.
- 3.35 In consideration of the original criteria and objectives of the program, the areas on which follow-up should focus are: (i) the effectiveness of the program approach; (ii) annual progress in municipal tax sharing systems in comparison with the recommendations of the MSS; (iii) the extent to which actions financed under institutional development contracts have been implemented; (iv) the program's impact on the administrative, operating, and fiscal situation of the municipalities; (v) the program's impact on the coverage and quality of municipal services, including services transferred to the cities by the provinces; (vi) costs of the projects and institutional development activities financed; (vii) training for municipal employees; (viii) operation and maintenance of the services; (ix) cost recovery; and (x) program focus. The indicators and methods defined in the program execution manual, which is an integral part of the Operating Regulations, will be used for this purpose.
- 3.36 Staff time requirements for program follow-up have been estimated as 18 person-weeks at Headquarters, 60 person-weeks at the Country Office, and 24 person-weeks of consultant services during the execution period.

F. Ex post evaluation

- 3.37 The information compiled during follow-up on the program will be used in preparing the ex post evaluation.

G. Cost recognition

- 3.38 The executing agency has incurred costs in preparing the program — such as the surveys of the municipalities and the builders'

association - and has contracted consultants to prepare some of the projects in the sample. It is estimated that the costs incurred between July 1993 and the expected date on which the loan will be approved amount to the equivalent of US\$1.4 million, of which US\$300,000 were incurred prior to October 1993. Accordingly, it is recommended that costs be recognized up to the equivalent of US\$300,000 from the local contribution, and up to US\$1.1 million from the loan, since procurements and contracts have complied with requisites substantially similar to those recommended for inclusion in the loan contract.

H. Procurement of goods and services

- 3.39 Based on a representative sample of projects and the shortfalls in urban services, the distribution of program funds by component is expected to be as follows:

Civil works	US\$220 million
Equipment	US\$ 29.1 million
Project consulting services	US\$ 19 million
Institutional development consulting	US\$ 20 million

- 3.40 It is anticipated that close to 60% of consulting services will be performed by consulting companies and the remainder by individual consultants.
- 3.41 Bank procedures, which will form an integral part of the loan contract, will be followed for the procurement of goods and the construction of civil works to be financed with the proceeds of the loan.
- 3.42 Owing to the large number of consulting services required by the program and on the basis of the experience acquired by the PEUs in contracting under earlier loans, the executing agency will be delegated responsibility for the selection and contracting process for service contracts costing up to US\$200,000, without prior consultation with the Bank, which would verify the entire process through ex post sampling. The normal procedures required by the Bank would be used for contracts over US\$200,000.
- 3.43 The bid schedules will be drawn up semiannually as the municipalities present their loan requests.

I. Disbursements

- 3.44 Considering the nature of the operation, the volume of transactions that will take place as a consequence of goods and services procurement, and the fact that this is a global program, an efficient and rapid mechanism will be used to streamline the process of disbursing the program's funds.

- 3.45 Disbursements will follow Bank rules, except for justifications of advances and reimbursements of payments made, which would only require the executing agency to submit a disbursement request to the Bank's Country Office, accompanied by the breakdown of payments and control of disbursements and local contributions, with the supporting documentation remaining in the possession of the executing agency.
- 3.46 The executing agency will ensure that the information contained in the breakdown of payments is duly substantiated with the evidence normally required by the Bank. The executing agency will retain the originals and/or copies of the contracts, purchase orders, bills, receipts, proof of payment, suppliers' certificates, certificates of origin, and other documents supporting the information provided in the breakdown of payments. The documentation must be duly identified, properly filed, and available for review by IDB officers and external auditors. The documentation in question will be kept in an active file, in a place determined by the executing agency, for not less than five years counting from the date of the final disbursement of the Bank loan.
- 3.47 During its inspection visits, the Country Office will sample the documentation supporting the disbursements for review purposes. When the technical and/or financial inspections are carried out, samples will be examined to ensure that the supporting documentation for disbursement requests is available and that the funds whose reimbursement was requested have been used in accordance with the loan contract. Should errors be found, a larger percentage of documentation will be checked and the executing agency notified for the purpose of making the corresponding deductions from future requests.

J. Use of recoveries

- 3.48 Funds recovered from the loans granted under the program in excess of the amounts required to service them, may only be used to grant new loans under conditions that are substantially similar to the requirements established in the loan contract and the Operating Regulations, unless the Bank and the borrower agree to put the recoveries to a different use in keeping with the basic objectives of the financing.

K. Auditing

- 3.49 Beginning in the year in which the program gets underway and throughout execution, the program's financial statements must be submitted annually within the first four months after the end of each financial year, certified by independent external auditors. Their report will include an opinion regarding the annual follow-up report on the program on aspects agreed upon with the Bank.

IV. THE BORROWER AND THE EXECUTING AGENCY

A. The borrower

- 4.1 The borrower will be the Argentine Republic, which will designate the Department of the Secretary of Social Development (SDS) which reports to the Office of the President of the Republic as the executing agency. The SDS will execute the program through the Office of the Under Secretary of Housing, where the national coordinating unit (NCU) is located.

B. The executing agencies

1. Office of the Under Secretary of Housing (SSV)

- 4.2 To execute the program, the SSV has the NCU that was established to execute the global urban development program financed by the Bank, and which was successful in overcoming a slow start owing to macroeconomic stability, political changes, and difficulties in obtaining local counterpart funding on time.
- 4.3 Aside from the experience it has gained in executing the previous operation, the NCU has demonstrated its capacity to promote and manage the planning of projects, studies, and other background information required to prepare the program under discussion here. Its staff has technical expertise, its administrative systems are sound, and its infrastructure is geared to its functions.
- 4.4 The NCU is composed of one executive coordinator, two senior engineers, two junior engineers, two senior economists, one junior economist, one senior attorney, one senior financial analyst, two junior financial analysts, one senior specialist in institutional development, one junior specialist in institutional development, and five support staff. It would also be possible to hire consultants in peak evaluation and supervision periods.
- 4.5 To formalize the NCU as the program executing unit with all the respective legal powers, the borrower, as a prior condition to the first disbursement, must demonstrate to the Bank's satisfaction that it has established a program executing unit in the SSV.

2. Provincial executing units (PEUs)

- 4.6 The PEUs will be responsible for program supervision and execution in their respective provinces. They will be given sufficient authority to coordinate and supervise project execution in their territory. Initially, the provinces will use the PEUs set up to execute the program for financial rehabilitation and economic development for the Argentine provinces, tapping their experience in programs of this kind.

- 4.7 The PEUs are staffed with personnel that have sufficient professional experience to execute the program, and the NCU will provide consultants to strengthen them in the application of the evaluation methods established for the program.
- 4.8 In addition, the PEUs will use consulting services to assist with the largest and/or more specialized tasks they are called upon to perform in executing the program and/or specific projects. Since the PEUs will be set up in accordance with the needs of each province, the provincial governments may set up a specific PEU to execute this program, with the NCU recommending the staff roster needed for the smooth functioning of each PEU.
- 4.9 The roster will vary depending on the demand in each province and the suggested numbers for three sizes of PEUs are seven, fourteen, and twenty-two people, including professionals and support staff.

V. PROGRAM JUSTIFICATION, FEASIBILITY, AND RISKS

A. Justification

- 5.1 The main justification for the program is that it forms part, in the municipal area, of the process of structural change being carried out in Argentina. The process seeks to make the municipalities effectively autonomous, which should be accompanied by a clear delegation of responsibilities in investment decisions and in the provision of services.
- 5.2 The program will make it possible to continue and deepen the process of transparency and efficiency in intergovernmental transfers of resources, the mobilization of local resources, and in the targeting of subsidies. The idea is to set up a system in which: (i) a new municipal tax sharing system will be established; (ii) the investment, operating, and maintenance costs of the works will be recovered from the direct beneficiaries; and (iii) subsidies, if required, will be rationalized and budgeted for, and targeted directly to low-income groups.
- 5.3 These actions will bring additional economic benefits over and above those stemming strictly from the projects financed. These aggregate benefits stem from better allocation of financial resources and transparency in their use, greater investment efficiency owing to tighter financial discipline, greater mobilization of resources, and a more rational system for allocating subsidies.
- 5.4 All of these changes are conducive to an increase in the availability and productivity of productive resources which, in turn, increases the growth capacity of the economy. This group of benefits, although real and large, cannot be quantified. Nonetheless, they can be added to the benefits expected from the planned investments, which are identified below.

B. Program feasibility

1. Representative sample

- 5.5 The investment component will be executed by municipal governments and municipal companies that meet the eligibility criteria. To establish the size and possible make-up of this component, the SDS conducted a study on the autonomy and sphere of action of the municipalities, based on a statistically-representative sample of 109 municipalities. The study involved 13 municipalities with populations of over 200,000, 26 with populations between 200,000 and 50,000, and 70 with populations under 50,000.

- 5.6 The study identified 782 potential projects of which 630 were eligible for program financing. Thirty-five representative projects with more advanced studies and designs were selected from this sample. Their technical, financial, economic, and environmental aspects were studied in detail to constitute the representative sample for the program, and the results are presented in Table V-1.
- 5.7 The program funds would principally be used to finance the sectors mentioned below, which were included in the sample at the costs indicated in parenthesis:
- a. Urban facilities (US\$23.3 million) including daycare facilities, bus terminals, parks, green areas, and recreational areas.
 - b. Sanitation projects (US\$44.9 million) including flood protection, storm sewers, and solid waste projects.
 - c. City streets (US\$30.2 million) including paving and supplementary works.
 - d. Public lighting (US\$2.1 million) including new installations and the expansion of existing systems.
 - e. Neighborhood improvement (US\$3.6 million) includes basic infrastructure, sanitary cores, and multiple-use rooms, as pertinent.
- 5.8 An analysis of the 35 projects in the sample showed that 29 complied with the eligibility criteria, five had to be postponed, and one did not have complete documentation. The results of the analysis of the 35 projects are presented in Table V-1. ^{2/} For each project the table includes geographic location, investment, operating, and maintenance costs, the main alternatives considered during the evaluation process, the methodology used to estimate benefits, the internal rate of economic return (IRER), the eligibility coefficient for the municipality, the main cost recovery criteria, and the distributional impact.

^{2/} Of these 29 projects, nine are located in provinces that would be chosen by the Argentine authorities for a future municipal program with the World Bank.

TABLE V-1
MAIN FEATURES OF THE SAMPLE OF PROJECTS

	Municipality	Type of work	Costs (US\$000)		Analysis of alternatives	Economic evaluation method	IRER (%)	Mun.Blg. (income/costs)	Cost recovery system
			Invest.	Ops. and Maint.					
Children	Comod. Rivadavia	5 kindergartens with community center	3,219.0	1,340.8	Location, use, design, and materials	Cost-efficiency	N.A.	1.22	General revenues
	Guaymallen	7 daycare centers	1,628.2	1,342.6	Location, design, and materials	Cost-efficiency	N.A.	1.44	Gen. rev. & provinc. contr.
	Alberdi	Community center	617.7	160.5	Location, design, and materials	Cost-efficiency	N.A.	1.13	Postponed-overscaled
	Lules	Community center	560.8	107.9	Location, design, and materials	Cost-efficiency	N.A.	1.07	Postponed-overscaled
	Monteros	Bus terminal	1,353.5	105.2	Location and design	Private evaluation	21.4	1.26	User fees and rentals
	Rafaela	Bus terminal	1,366.9	124.1	Location and design	Private evaluation	20.4	1.51	User fees and rentals
Recreation areas	San Martín	Multiple sports complex	1,669.9	710.1	Design, uses, and materials	Cost-efficiency	N.A.	1.05	User fees and provinc. contr.
	Godoy Cruz	Forest park, 12 hectares	3,465.1	136.5	Location	Willingness to pay	18.2	1.12	Increase in CMC*
	Córdoba	2 forest parks	4,042.5	456.0	Location and type of park	Willingness to pay	40.6	1.53	Increase in CMC*
	La Rioja	Forest park	2,815.2	93.9	Location and type of park	Willingness to pay	30.6	0.27	Postponed-ineligible munic.
	Stgo. del Estero	2 parks (1 with sports area)	2,815.6	89.7	Location and type of park	Willingness to pay	26.9	1.17	Increase in CMC*
	C. del Uruguay	Dike and pumping plant	3,192.7	83.9	Location of dikes	Damage avoided	18.5	1.19	Improvement tax
	Catamarca	Drains and collectors, north	532.3	22.3	Recurrence and sections, layout	Damage avoided	21.7	1.77	Improvement tax
	Pto. Madryn	Drains and collectors, entire city	5,090.5	37.7	Recurrence and sections, layout	Damage avoided	17.1	1.29	Improvement tax
	Carlos Casares	Collectors throughout the city	6,203.2	44.1	Layout, materials and sections	Shadow prices	47.0	1.17	Improv. tax and gen. revenue
	Río Cuarto	Stages 2, 3, and 4, south part of the city	9,174.2	60.0	Layout, materials and sections	Willingness to pay	25.4	1.33	Improv. tax and gen. revenue
	Córdoba	Collect.netwrk. Alta Córdoba and Arguello	10,560.8	60.0	Layout, materials and sections	Willingness to pay	34.9	1.53	Improv. tax and gen. revenue
	Villa del Rosario	Collector network throughout the city	2,526.9	5.4	Layout, materials and sections	Willingness to pay	16.2	1.17	Improv. tax
	Cerrillos	Collector network and canal	817.5	2.5	Collector points and materials	Willingness to pay	46.4	1.73	Improv. tax and CMC*
	Concordia	Collector network and improv. to canal	2,993.8	24.0	Recurrence, sections and materials	Damage avoided	21.8	1.31	Improv. tax and CMC*
	Paso de los Libres	Collector network throughout the city	1,095.1	21.1	Layout, materials and sections	Willingness to pay	19.6	1.65	Improv. tax and gen. revenue
	Villa Regina	Collector network throughout the city	2,000.0	6.5	Unavailable	Unavailable	unavailable	2.19	Postponed-incompl. docum.
	Villa Regina	Solid waste recycling plant	639.1	221.3	Loc.and compar.with sanit. landfill	Cost-efficiency	N/A	2.19	Sale of prod. and gen. revenue
	Bahía Blanca	Vehicle bridge over railway line	3,855.3	N/A	Location, design and structure	Cost savings	17.3	1.22	Postponed-incompl. docum.
	Belville	Pavement, storm drains and vehicle bridge	2,276.6	14.1	Type of pavement and loc.of bridge	Willingness to pay	24.4	1.26	Improv. tax and gen. revenue
	Marcos Juárez	Pavement, lighting and sewers	2,621.3	45.0	Type of lighting & pavement	Willingness to pay	14.1	1.43	Improvement tax
	Crespo	Paving of 97 blocks	3,183.0	11.8	Type of pavement	Willingness to pay	13.5	1.54	Improv. tax and gen. revenue
	Nogoya	Paving of 200 blocks	5,326.2	22.0	Design st. syst. and type of pavemt.	Willingness to pay	37.9	1.23	Improvement and property
	San Luis	Paving of 70 blocks	2,171.1	174.9	Design st. syst. and type of pavemt.	Cost savings	21.1	1.27	Automobile license
	Tupungato	Paving of 70 blocks	1,301.1	5.8	Design st. syst. and type of pavemt.	Willingness to pay	21.1	1.21	Improv. tax and gen. revenue
	Constitución	Pavement and storm sewers for 190 blocks	4,721.8	11.7	Type of pavement	Willingness to pay	12.2	1.29	Improv. tax and gen. revenue
	Viedma	Pavement and storm sewers for 108 blocks	4,793.1	13.7	Design st. syst. and type of pavemt.	Willingness to pay	17.1	1.06	Improv. tax and gen. revenue
	Allen	Improved lighting, 200 blocks	963.9	104.8	Type of lighting & electric circuit	Costs saved and WTP	37.1	1.10	Improv. tax
	San Juan	Improved lighting, 230 blocks	1,129.7	193.7	Type of lighting & electric circuit	Willingness to pay	21.8	1.09	Improv. tax
Improvement	Bariloche	Kitchen & bath, paving and kindergarten	3,663.4	56.4	Design and type of solution	WTP and minimum cost	N/A	1.14	Improv. tax and subsidy
Sample presented:			(US\$ 000) 104,387.0 (does not include taxes)						
Sample:			(US\$ 000) 94,538.0 (does not include taxes)		Weighted total for distributional impact:				

CMC = city maintenance charges

2. Benefits and economic feasibility

- 5.9 The projects to be financed under the program will produce local services to improve the quality of life in the communities. The increase in coverage of such services will generally take place in low-income sectors as is indicated in the analysis of the distributional impact of the sample. Job creation is an additional benefit for these groups. Based on the information for the projects in the sample regarding use of unskilled labor, it is estimated that the program will create the equivalent of 110,000 person-months of work related to the investments for unskilled laborers.
- 5.10 To analyze the economic feasibility of the works, socioeconomic evaluations were performed on the 35 projects in the sample. Cost-benefit was used to study 27 projects, 7 were studied on the basis of scaling and minimum cost solution, while one did not have sufficient information to produce reliable results.
- 5.11 The cost-benefit analysis included a study of: (i) supply and demand for the services to be provided under each of the projects in order to be sure that they were properly scaled; (ii) alternatives to ensure that the one selected was the minimum cost solution; and (iii) cost-benefit in order to establish whether the internal rate of economic return (IRER) for each project was over 12%, which is the figure used as a proxy for the social opportunity of cost of capital.
- 5.12 A sensitivity analysis was conducted for each project. Since designs were only available at the preproject level, a figure of 20% was taken for possible variations in cost for projects with a major excavation component, and 15% for the other projects.
- 5.13 A figure of 20% was used as the variance range on the benefit side. In cases in which the standard deviation for willingness to pay was an important cost factor, 25% was taken as the value for the reduction of benefits. Despite these changes in the variables, the projects analyzed continued to have IRERs of over 12%.
- 5.14 The weighted average (by the investment cost) of the IRERs for the sample as a whole is 26.2%. The IRERs per component are shown in Table V-2.

TABLE V-2
Returns on the projects in the sample

TYPE OF WORK	IRER (%)
I. Urban facilities	28.1
1.1 Bus terminals	20.9
1.2 Parks, green areas, and recreation areas	29.6
II. Sanitation	28.8
2.1 Flood protection	17.9
2.2 Storm sewers	31.7
III. City streets	17.8
IV. Lighting	28.8

- 5.15 For projects whose benefits could not be quantified, supply and demand for the proposed service was analyzed for each component in function of existing and projected population figures, and public requirements. Representative surveys were conducted of the needs voiced by the beneficiary population and a check was made to ensure that the project location was accessible to the community and that the proposed physical design would minimize the present value of the investment, operating, and maintenance costs, at the rate of 12%.

3. Technical and environmental feasibility

- 5.16 The technical feasibility study of the sample of projects and of the municipalities indicates that there is sufficient consulting capacity to carry out the works component in keeping with the program's eligibility criteria and technical requisites.
- 5.17 The analysis of the projects in the sample verified that the plans were prepared taking account of alternatives for location, layout, materials, and technologies, in order to obtain the least-cost solution with regard to investment, as well as operating and maintenance costs.
- 5.18 On the construction side, the works in the program are routine, and no complex works are envisaged. The capacity and experience of the Argentine construction sector is more than sufficient to execute works of this kind, as is apparent from the large- and medium-sized projects that are being carried out in the country.
- 5.19 As for the environmental impact of the projects, actions of this type always have a positive impact on the physical aspects and quality of life in communities, both at the project site and in its

area of influence. However, there are some infrastructure works which owing to their very nature present environmental risks in some of the stages of construction, operation, or maintenance.

- 5.20 To reduce or mitigate negative environmental impact, the Department of the Secretary of Social Development prepared procedures for the control of the environmental quality of the projects to be financed under the program, whose guidelines were agreed upon with the Bank. These procedures will form part of the program's Operating Regulations.
- 5.21 The CMA classified this program in Category III at its meeting on November 16, 1992, and the environmental summary was considered by the Committee on October 20, 1993. The recommendations made on those occasions have been followed in designing this program.

4. Institutional and financial feasibility

- 5.22 The institutional development component should make it possible to carry out the program satisfactorily within the term planned for its execution, despite the institutional weakness of the municipalities.
- 5.23 The financial feasibility of the program is based on full cost recovery which means that the beneficiaries must be willing to pay. When the operation was designed, the direct and indirect beneficiaries were identified, classified in function of the size of benefits they would receive, and when warranted, their willingness to pay for the service was measured. Based on the results, mechanisms were designed to recover the costs of the investment, and of operating and maintaining the works.
- 5.24 The diagnosis of the municipalities was used to prepare financial projections, starting with a per capita level of municipal revenues per year of US\$130, and rising to a level of US\$163 by 1999 (25.4% real increase) and US\$176 by the year 2002 (35.4% real increase over the base year).
- 5.25 The projections are based on a very conservative policy for recurrent expenses in general, since the program to correct institutional weaknesses will lead to large savings as a result of improved efficiency in organization, management control, and other structural changes.
- 5.26 As a consequence of the above, growth in real per capita investment will be significant, rising from an annual average of US\$32 to US\$76 in 1999 and US\$92 in 2002.
- 5.27 These figures indicate that the municipalities, on the basis of stricter fiscal discipline and better internal mobilization of resources, will be able to obtain the funding required to carry out

the program's works as well as additional works required by the community.

C. Distributional impact

- 5.28 The distributional impact coefficient (DIC) was obtained by calculating the percentage of private-sector benefits from each project that will go to low-income groups. ^{3/} The difference between wages paid by the projects and the opportunity costs of unskilled labor was also considered as part of the benefits going to low-income groups.
- 5.29 As shown in Table V-1, the distributional impact indicator ranges from 47% to 100%. The weighted average (by the cost of the investment) for the projects analyzed was 66.9%. The results for these projects and the types of investments to be financed under the program indicate that much more than 50% of the program benefits will accrue to low-income groups.
- 5.30 In keeping with the guidelines contained in the document on the Eighth Replenishment of Resources, this program can be classified as targeted to low-income groups since it focuses on the poorest provinces, where most of its benefits will go to those groups.

D. Impact on women's development

- 5.31 The program will make a considerable contribution to the development of women, since the works included in it provide direct benefits such as kindergartens and mother and child facilities where over 30% of the users are families headed by women. The community centers and recreational areas also have a direct benefit for women. The other components improve the quality of life of families, and therefore this benefit is also received by women.

E. Program risks

- 5.32 In the process of State reform, especially with regard to the decentralization of functions to the provincial and particularly to the local governments, the institutional frameworks have experienced changes and are still in transition. Provincial and municipal legislation must be made to reflect these changes. Should this not be done in a timely fashion, the benefits of the program which derive from the systematization of fiscal relations between the provincial and municipal governments could be affected. To minimize this risk, the program envisages that the Bank and the national coordinating unit will convince the provinces to adopt suitable municipal tax sharing systems. At the annual review meetings the Bank will assess the headway made in this area.

^{3/} The low-income line for Argentina as of June 1993 was equivalent to US\$1,929 per capita each year.

- 5.33 Institutional and operational weaknesses, compounded by shortcomings in staffing structure and numbers, stand in the way of good administration and management of local services. The MSS and the institutional development program will pay special attention to these aspects in order to minimize the risks.
- 5.34 A further risk is posed by the possibility of political favoritism in the provinces which might restrict the program's benefits to certain municipalities. To avoid this risk, the program makes the national coordinating unit responsible for hearing appeals brought by the municipalities regarding decisions made by the provincial executing units on the eligibility of municipalities and projects.
- 5.35 The government is considering a lending operation for the least-developed provinces. The coexistence of the proposed program with other lending operations that offer softer conditions could weaken or arrest program execution. Special care must be taken to ensure that future operations are compatible with the program.

PROPOSED RESOLUTION

ARGENTINA. LOAN ____/OC-AR. TO THE REPUBLIC OF ARGENTINA
(Program for Institutional Development and
Municipal Social Investments)

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 Republic of Argentina, as Borrower, for the purpose of granting it a financing to cooperate in the execution of a program for institutional development and municipal social investments. Such financing shall be for the amount of one hundred eighty million dollars of the United States of America (US\$180,000,000) or its equivalent in other currencies, except that of Argentina, which are part of the Ordinary Capital resources of the Bank. The financing shall be subject to the "Special Contractual Conditions" and the "Terms and Financial Conditions" of the Executive Summary of the Loan Proposal.

PROPOSED RESOLUTION

ARGENTINA. LOAN ____/SF-AR. TO THE REPUBLIC OF ARGENTINA
(Program for Institutional Development and
Municipal Social Investments)

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 Republic of Argentina, as Borrower, for the purpose of granting it a financing to cooperate in the execution of a program for institutional development and municipal social investments. Such financing shall be for the amount of thirty million dollars of the United States of America (US\$30,000,000) equivalent, in argentinean pesos, which are part of the resources of the Fund for Special Operations. This financing shall be subject to the "Special Contractual Conditions" and the "Terms and Financial Conditions" of the Executive Summary of the Loan Proposal.