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Report No. 88598-TN

PROGRAM APPRAISAL DOCUMENT

ON A

PROPOSED LOAN

IN THE AMOUNT OF EURO 217 MILLION
(US$300 MILLION EQUIVALENT)

TO THE

REPUBLIC OF TUNISIA

FOR THE

URBAN DEVELOPMENT AND LOCAL GOVERNANCE PROGRAM

June 27, 2014

Sustainable Development Department
MENA Region

CURRENCY EQUIVALENTS

(Exchange Rates Effective April 30, 2014)

Currency Unit	=	Tunisian Dinar (TND)
TND 1	=	US$0.63
US$1	=	TND 1.58
EUR 1	=	US$0.72

FISCAL YEAR

January 1 – December 31

ABBREVIATIONS AND ACRONYMS

AFD	French Development Agency */Agence Française de Développement*
ANPE	National Environmental Protection Agency/*Agence Nationale de Protection de l'Environnement*
ARRU	Urban Renovation and Rehabilitation Agency/*Agence de Rénovation et de Réhabilitation urbaine*
BCT	Central Bank of Tunisia*/ Banque Centrale de Tunisie*
CBG	Capital Block Grants
CFAD	Decentralization Support and Training Center/*Centre de Formation et d'appui à la Décentralisation*
CGSP	Controller General of Public Services/*Contrôleur Général des Services Publics*
COSEM	Market Monitoring Committee/*Comité de Suivi et d'Enquête sur les Marchés*
CPSCL	Municipal Development Fund/*Caisse des Prêts et de Soutien des Collectivités Locales*
CRC	Citizens' Report Card
CY	Calendar Year
DGCPL	General Directorate for Local Governments/*Direction Générale des Collectivités Publiques Locales*
DLI	Disbursement Linked Indicators
EIA	Environmental Impact Assessment
EIB	European Investment Bank
EMP	Environmental Management Plan
ERR	Economic Rate of Return
ESM	Environmental and Social Manual
ESMF	Environmental and Social Monitoring Framework
ESSA	Environmental and Social Systems Assessment
FCCL	Local Government Fund/*Fonds Commun des Collectivités Locales*
FDC	Cooperation Fund/*Fonds de Coopération*
FNVT	National Federation of Tunisian Cities/*Fédération Nationale des Villes Tunisiennes*
FRP	Financial Recovery Plans
GDP	Gross Domestic Product
GIZ	German Technical Assistance Cooperation
HICOP	Public Procurement Oversight Committee/*Haute Instance de la Commande*

	Publique
IGFT	Inter-Governmental Fiscal Transfer
IMC	Inter-Ministerial Committee
IPF	Investment Project Financing
ISN	Interim Strategy Note
IVA	Independent Verification Agent
LG	Local Government
LGCDP	Local Government Capacity Development Plan
MDCI	Ministry of Development and International Cooperation
MMC	Minimum Mandatory Conditions
MoEF	Ministry of Economy and Finance
MoI	Ministry of Interior
M&E	Monitoring and Evaluation
ONAS	National Sanitation Agency/*Office National de l'Assainissement*
OSR	Own Source Revenue
O&M	Operation and Maintenance
PA	Performance Assessment
PAP	Program Action Plan
PDM	Municipal Development Project
PforR	Program for Results
PIC	Municipal Investment Plan / *Plan d'Investissement Communal*
PDO	Program Development Objective
PNRQP	National Programs Targeting Upgrading of Disadvantaged Neighborhoods with the Provision of Basic Municipal Infrastructure
PPP	Public-Private Partnership
RPF	Resettlement Policy Framework
SD	Special Delegation
TA	Technical Assistance
TND	Tunisian Dinar
UDLGP	Urban Development and Local Governance Program

Regional Vice President:	Inger Andersen
Country Director:	Neil Simon Gray
Sector Director:	Junaid Kamal Ahmad
Sector Manager:	Franck Bousquet
Task Team Leader:	Jaafar Sadok Friaa

REPUBLIC OF TUNISIA

Urban Development and Local Government Program

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PAD DATA SHEET

Republic of Tunisia

Urban Development and Local Governance Project

PROGRAM APPRAISAL DOCUMENT

Middle East and North Africa Region
MNSSU

Basic Information

Date:	June 27, 2014	Sectors:	Urban
Country Director:	Neil Simon Gray	Themes:	Municipal Governance and institutional building, decentralization, public sector governance, urban development
Sector Manager/Director:	Franck Bousquet / Junaid Kamal Ahmad		
Program ID:	P130637		
Team Leader(s):	Jaafar Sadok Friaa		

Program Implementation Period: 5 years

Start Date: 07/24/2014
End Date: 06/30/2019

Expected Financing Effectiveness Date:
10/27/2014
Expected Financing Closing Date:
12/31/2019

Program Financing Data (US$M)

[X] Loan	[ ] Grant	[ ] Other
[ ] Credit		

For Loans/Credits/Others (US$M):

Total Program Cost	363	Total Bank Financing :	300
Total Cofinancing :		Financing Gap :	

Financing Source	**Amount** (US$M)
BORROWER	63
IBRD	300
Total	363

Borrower: Republic of Tunisia

Responsible Agency: Ministry of Economy and Finance

Contact:	Mme Khalthoum Hamzaoui	Title:	General Director, MEF
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Expected Disbursements (in USD Million)

Fiscal Year	2015	2016	2017	2018	2019	2020			
Annual	55.8	51	60.4	67.9	48.8	16.4			
Cumulative	55.8	106.8	167.2	234.8	283.6	300			

Program Development Objective(s)

The objectives of the Program are: (i) to strengthen Local Governments' performance to deliver municipal infrastructure, and (ii) to improve access to services in targeted disadvantaged neighborhoods.

Compliance

Policy

Does the program depart from the CAS in content or in other significant respects?	Yes [ ]	No [X]
Does the program require any waivers of Bank policies applicable to Program-for-Results operations?	Yes [ ]	No [X]
Have these been approved by Bank management?	Yes [ ]	No [ ]
Is approval for any policy waiver sought from the Board?	Yes [ ]	No [X]
Does the program meet the Regional criteria for readiness for implementation?	Yes [X]	No [ ]

Overall Risk Rating: High

Legal Conditions and Covenants

Name	Recurrent	Due Date	Frequency
Adoption of the Decree Legal Agreement Reference V	No	Effectiveness	Once

Description of Condition

The Decree, in form and substance acceptable to the Bank, has been adopted by the Borrower and published in the Borrower's National Gazette.

Name	Recurrent	Due Date	Frequency
Adoption of the Program Operations Manual Legal Agreement Reference V	No	Effectiveness	Once

Description of Condition

The Program Operations Manual, in form and substance satisfactory to the Bank, has been adopted by the Borrower.

Name	Recurrent	Due Date	Frequency
Procurement Audit Legal Agreement Reference Section III.C. of Schedule 2	Yes	No later than six months after the end of the FY to which said audit relates	Annual

Description of Covenant

The Borrower shall (a) carry out an audit of contracts procured in the preceding FY and furnish said audit to the Bank; and (b) ensure that the findings of said audit are taken into account in the Annual Performance Assessment for the FY to which said audit relates.

Team Composition				
Bank Staff				
Name	**Title**	**Specialization**	**Unit**	**UPI**
Jaafar Friaa	Lead Urban Specialist	TTL	MNSSU	
Augustin Maria	Senior Urban Specialist	Urban development	SASDU	
Eric Ranjeva	Finance Officer	Finance	CTRLA	
Henri Nkuepo	Counsel	Law	LEGAM	
Renaud Paubelle	Infrastructure Specialist	Technical and institutional	MNSSU	
Ayah Mahjoub	Economist	Development Economy	MNSSU	
Carolyn Winter	Senior Social Development Specialist	Social accountability and local governance	MNSSU	
Salim Benouniche	Lead Procurement Specialist	Procurement	MNAPR	
Walid Dhouibi	Procurement Specialist	Procurement	MNAPR	
Vincent Roquet	Social Development Specialist	Social Safeguards		
Taoufiq Bennouna	Senior Environmental Specialist	Environmental Safeguards	MNSSD	
Rama Krishnan	Lead Financial Management Specialist	Fiduciary Systems Assessment, Governance and Inter-Governmental Transfer	MNAFM	
Franck Bessette	Senior Financial Management Specialist	Financial Management	MNAFM	
Sophie Hans-Moevi	Program Assistant		MNSSU	
Guido Licciardi	Urban Specialist	Urban Specialist	FEU	
Non Bank Staff				
Name	**Title**	**Office Phone**	**City**	
Jeffrey Racki	Decentralization and municipal development expert			
Sherif Arif	Environmental safeguards expert			
Mohamed Mehdi	Financial management expert			
Charles Malecot	Municipal finance expert			
Mohamed Ghourabi	Environmental and social specialist			

I. STRATEGIC CONTEXT

A. Country Context

1. **Tunisia is currently going through a transitional phase of democratic and political reform**. In January 2011, the wave of protests that ended the 23-year rule of President Zine El Abidine Ben Ali ushered in a new political, social and economic era. The revolution was fueled by widespread anger and frustration over lack of social and political inclusion, governance and corruption, mounting unemployment and the rising cost of living. Since then, Tunisia successfully held its first democratic elections for a National Constituent Assembly in October 2011.

2. **Tunisia's political transition gained new momentum in early 2014, with the resolution of a political deadlock, the adoption of a new Constitution and the appointment of a new Government.** The national dialogue platform, brokered by key civil society organizations, played a crucial role in gathering all major political parties. This resulted in the adoption of a consensual roadmap leading to general elections, planned for the end of 2014. Additionally, local elections (municipal and regional) are expected to be organized in 2015. The strategic direction that the new Government embarked upon focuses on restoring and maintaining security, while laying the groundwork for a stronger economic recovery, key to successfully completing the democratic transition.

3. **After a short-lived rebound in 2012 and throughout 2013, increasing political and social instability, as well as a difficult external environment, have led to a slowdown in economic growth.** Rebounding from the contraction of 1.9 percent of GDP in 2011, the economy grew by 3.6 percent in 2012, somewhat above expectations. For 2013, growth was estimated to have slowed to 2.6 percent, as agricultural production, as well as the oil and gas sector, declined markedly, and manufacturing stagnated. Unemployment continued to decline to 15.3 percent at the end of 2013, from 16.7 percent one year earlier, but was still well above the pre-revolution level of 13 percent. Post-revolutionary Governments pursued expansionary fiscal and monetary policies until 2013 as an effort to support economic recovery and employment. In 2013, the deficit reached six percent. A tightening of monetary policies as well as more moderate commodity prices have allowed for a slowdown in consumer price inflation, which fell to 5.5 percent in February 2014, after having reached 6.3 percent in 2013.

4. **Although poverty in Tunisia decreased by nearly half between 2000 and 2010 and the country performed well across a range of social indicators, regional disparities saw poverty rates in excess of 30 percent in some parts of the country.** High unemployment was a major driver of the 2011 revolution, particularly among the young who failed to reap the benefits of relatively buoyant growth. While Tunisia is one of the more advanced countries in the region, underutilization of skilled women in the labor market remains a concern, and addressing women's rights more generally represents a key governance issue. In the short term, the Government's main challenge will be to ensure social peace and security as a prerequisite for restoring economic activity and putting the economy back onto a growth trajectory. The Government is also seeking to establish an enabling environment for structural reforms which, among other objectives, would reduce unemployment and regional disparities, introduce participatory governance, and improve living conditions throughout the country.

5. **Today, Tunisian policymakers are rethinking the relationship between central and local Governments (LGs), and have taken concrete steps towards a more decentralized system**. Since the January 2011 revolution, Tunisia has signaled its intent to bring cities into the heart of the local development process, making them proactive players in planning, implementing and delivering municipal infrastructure and services. There is widespread recognition that LGs[1], with their elected

[1] Under the present Program, LG means Municipality.

municipal councils and mayors, must be more than “passive spectators” in urban development. Moreover, there is a general consensus that LGs need to become more transparent and accountable to local citizens.

6. **The New Constitution promulgated on Jan 27, 2014, includes clear commitments to decentralization** and proposes fully devolved and empowered LGs with autonomy for executing their mandates of providing local services according to transparent principles of participation by, and accountability to, their citizens. The changes mandated by the Constitution regarding local governance are transformational, as they effectively reverse the highly centralized previous structure, whereby central oversight and approval (“*tutelle*”) was exercised on all facets of Local Government accountability, decision-making, and capital works and service delivery-related investments. The Constitution recognizes the decentralization processes as the fundamental basis for the organization and distribution of power in Tunisia, and as an essential step to achieve an administration that is more responsive and accountable to citizens. The first article dedicated to LGs states that "local power is based on decentralization" (Chapter VII, Article 131). It further states that LGs (particularly municipalities and regional governments) are chosen by universal, free and transparent vote, and will have their own legal personality, together with administrative and financial independence.

B. Sectoral and Institutional Context

7. **Tunisia is one of the most urbanized countries in the Middle East and North Africa**. In 1975, the country’s rate of urbanization was already 50 percent; today, roughly 70 percent of the country’s eleven million citizens live in towns and cities, most of them on the coastal Mediterranean belt. Tunisia’s urban sector is the most vibrant contributor to the national economy, accounting for more than 85 percent of the country’s GDP. Approximately 56 percent of the population and nine out of ten Tunisian industrial firms are located within an hour’s travel time from Tunisia’s three largest cities: Tunis (the capital), Sfax and Sousse. These three coastal cities are the centers of economic activity, accounting for 66 percent of the country’s GDP.

8. If Tunisian municipalities are very different in terms of size[2], they all share – to varying degrees – some common attributes**: they have few responsibilities, play a relatively minor role in urban/local development, enjoy limited decision-making powers, and currently have a limited connection with their citizens.** Their economic contribution has been growing during the last decade at a slower rate than the overall economy and presently accounts for about 1.2 percent of GDP (and less than four percent of total public expenditures), compared with 15 percent in Morocco and 20 percent in Turkey. The national Government spends TND 2,000 per capita (operating costs and investments combined) while municipalities spend TND 75 per capita. Moreover, there has been a downward trend in the relative weight of municipal expenditure between 2002 and 2012. While GDP increased 7.1 percent and the national budget grew nine percent a year, municipal revenues increased only 6.1 percent a year—only about one percent above the inflation and demographic growth rates. In parallel, municipal investments have been shrinking. Between 2002 and 2012, they declined by two percent and amounted to only two percent of all Government investments.

9. **Tunisia has a long tradition of LGs, governed by elected municipal councils, and with a formally clear set of responsibilities. However, a highly centralized oversight system of “*tutelle*” has sharply constrained their decision-making and independence.** Under normal circumstances, Tunisian municipalities are governed by a council, directly elected for a five-year mandate, and an

executive headed by the mayor, elected among the councilors (except Tunis, where the mayor is named by decree among the councilors). The most recent municipal elections were held in May 2010 – but following the January 2011 Revolution, all municipal councils were dissolved and replaced by Special Delegations (SDs), members of which were nominated by Prime Minister Decree. It is expected that new councils will replace the SDs following the next set of local elections, scheduled for 2015. Elected municipal councils and mayors, however, were always subject to administrative supervision (or "*tutelle*"), whereby key LG decisions (such as annual budgets, by-laws, etc.) required approval from the State (in one form or another) before becoming effective. The powers of SDs – which do not enjoy electoral legitimacy – are even more circumscribed. Historically, and in the shadow of first a colonial and then a centralized state, Tunisian municipalities have not provided much in the way of "invited spaces", within which citizens have been able to engage meaningfully with the "local state" or to voice their preferences and priorities. Issues of accountability and participation have now come to the fore, gaining added importance in the wake of a post-revolutionary crisis of political legitimacy, and a general deterioration in municipal services.

10. **De facto, LGs in Tunisia have limited functional responsibilities**. Apart from administrative and vital registration services, the most important services delivered by municipalities are municipal solid waste collection and the construction and maintenance of municipal road networks. They are also responsible for urban parks, some cultural and sports facilities, and a few commercial facilities (such as food markets and slaughterhouses). Provision of electricity, water, wastewater and urban transport are all under the responsibility of the central Government. In each of these areas, several key actors are involved (such as sector ministries or specialized agencies), with a limited consultative role devolved to LGs. In a relatively small country, this highly centralized, post-independence model of public investments has indeed provided most Tunisians with good access to basic infrastructure. However, centralization now appears to be inappropriate given the relative economic maturity of the country, political changes, greater local capacities, infrastructure maintenance requirements, and the need to sustain and improve the quality of services in a sustainable manner.

11. **Municipal expenditures are dominated by spending in two sectors: municipal solid waste collection and street networks** (construction and maintenance) which together account for approximately 80 percent of total municipal expenditures (recurrent and capital). Municipal expenditure, by all accounts, is inefficient and does not lead to quality and sustainability of services. Many activities are carried out through force accounts ("*en régie*"), resulting in inflated payroll commitments while at the same time under-spending on other Operation and Maintenance tasks. For instance, it is estimated that up to 70 percent of municipal equipment (vehicles, etc.) is currently out-of-order, leading to worsening waste collection services and a visible increase in litter on residential and other roads and pavements. At the municipal level, all investment needs are systematized within Municipal Investment Plans (PIC).

12. **At the national level, municipalities are regulated and monitored by the General Directorate of Local Governments (DGPCL)**, a key directorate within the Ministry of the Interior. In addition to its regulatory functions, the DGPCL is also responsible for managing the Local Government Common Fund (FCCL, *Fonds Commun des Collectivités Locales*), which provides LGs with annual block grants to support their operating budgets. Besides the Municipal Development Fund (CPSCL, *Caisse des Prêts et de Soutien des Collectivités Locales*), which is primarily accountable to the Ministry of Interior and the Ministry of Finance, is a separate entity providing LGs with access to credit as well as to central Government funding to finance municipal investments (loans and capital grants).

13. **As in all inter-governmental fiscal systems, that of Tunisia has always included an important center-to-local transfer component**. The clearest element of this Inter-Governmental Fiscal Transfer

(IGFT) system has been the FCCL, managed by the DGPCL. The total budget envelope of the FCCL is decided every year and then allocated to all municipalities on the basis of a formula. FCCL allocations to municipalities are, in effect, general purpose block grants, the use of which is entirely at the discretion of municipalities. The total size of the FCCL (of which the funding pool set aside for communal allocations represents a little over 70 percent[3]) has been growing in recent years, increasing from around US$103 million in 2008 to a little over US$160 million in 2012[4]. Municipalities' Own Source Revenues (OSR) have increased on average by 5.5 percent per year during the 2002-2012 period and have not kept pace with the recent increase in recurrent expenditure. Among the direct taxes are property taxes, the rental value tax on housing (paid by owners) and the tax on unbuilt land, both levied at a rate of 0.3 percent (which was decreased from 0.6 percent in 1996).[5]

14. **The structure of the current capital grant system adds to LGs' fiscal stress and disproportionately favors stronger LGs.** Municipal revenues and expenditures are classified into recurrent (Title 1 – T1) and capital (Title 2 – T2). The table below presents the evolution of aggregate municipal budgets over the 2002-2012 period.

Table 1: Aggregate Municipal Budgets 2002-2012 in million TDN

Year	02	03	04	05	06	07	08	09	10	11	12
Recurrent revenues / T1	309	324	351	374	409	427	458	479	536	561	641
Own Source Revenues	223	234	258	279	312	322	346	360	404	268	370
FCCL	86	90	92	95	98	105	112	119	131	145	176
Exceptional transfers	0	0	0	0	0	0	0	0	0	148	95
Recurrent Expenditure / T1	258	272	289	306	332	350	376	403	428	460	502
Capital resources / T2	160	137	166	166	154	159	170	235	246	218	228
Capital Expenditures / T2	154	130	166	160	149	141	132	188	194	140	129
Investments	129	98	135	126	115	101	89	144	146	87	59
Capital Reimbursement	25	32	31	34	34	40	43	45	48	54	60

Source: DGCPL and CPSCL

[3] The rest (some 30 percent) is being reserved for allocations to regional councils, the Tunis municipality, governorates, etc.
[4] In addition, the Government also provided supplementary transfers to all municipalities of US$95 million in 2011 and US$64 million in 2012.
[5] Vaillancourt 2008.

15. **LGs face the increasingly serious issue of growing municipal debt, driven largely by the requirement that they borrow from the CPSCL to finance their capital investments.** Consequently, although LGs appear to have relatively stable net operating surpluses at around nine percent of recurrent revenues, the extent of the problem is hidden by repeated rescheduling of the debt under the direction of the Ministry of Economy and Finance, and by supplements provided through exceptional transfers to cover increasing recurrent costs, including debt obligations to the CPSCL for investment loans (exceptional transfers are now regularized through the newly created *Fond de Cooperation* – FDC). Current LG arrears on CPSCL loans are illustrative. Over 120 LGs are in arrears of 90 days or more, and of these, 80 LGs owe amounts in excess of TND 250,000 (equivalent to US$167,000). Over 30 LGs are considered chronically indebted and unable to retire their debts. In addition to the financial implications of the debt, the response to dealing with it includes: relaxing the loan to grant ratios; introducing new operating grant transfer instruments; and providing exceptional transfers. In addition, those LGs capable of raising larger amounts of OSRs and of servicing larger loans have increasingly commanded a larger share of grant allocations on a per capita basis. All of these responses blur the clarity of the grant system and open it up to increasingly ad hoc functional arrangements.

Box 1: PIC Funding Sources and Municipal Debt Situation

Currently, CPSCL loan and capital grants for municipal investments are fairly rigidly linked together through financing arrangements defined by Municipal Investment Plans (PIC). The financing plan for each project under the PIC would be defined based on: (i) a maximum grant share depending on the type of project; (ii) the applicable lending terms; and (iii) the requirement for each municipality to contribute at least 10 percent from its own resources. However, over time this has led to high levels of municipal debt. By mid-2005, aggregate arrears on municipal debt repayments were 146 MDT (39% of current municipal revenues). Debt service had increased from 14 MDT to 40 MDT from 1993 to 2000, then to 56 MDT in 2005. The debt service ratio (interest + principal/current revenues) increased from 7.7% in 1993 to about 15% by 2005. These figures represent an aggregate situation for all municipalities, but clearly, CPSCL debt service, as well as arrears to suppliers and service providers had, by 2005, become financially untenable for many municipalities, particularly smaller ones.

Municipalities have subsequently restructured their debt several times—in 1997, 2002, and 2006—both for the loans contracted from the CPSCL and for non-payments to suppliers such as the National Water Exploitation and Distribution Company, the Tunisian Electricity and Gas Company, and Tunisia Telecom. In 2007 the arrears on municipal debt at the end-2006 were rescheduled for TND 66 million, and TND 29 million of it for Tunis (44%). Despite these measures, additional arrears totaling TND 16.7 million were generated in 2007, and by 2012, aggregate arrears on municipal debt had reached 150 million TND, two to three times the net savings of the 264 municipalities. The situation today has improved, in part thanks to the recent increase in national transfers, but the total municipal debts to the CPSCL reached TND87 million end of 2013.

16. **Beyond the formula-based allocation of the FCCL, the central Government also provides municipalities with capital budget transfers in the form of investment-by-investment capital grants, which are less predictable and transparent.** These capital grants are usually linked to municipal borrowing from the CPSCL and to the 5-year Municipal Investment Plan (the PIC, currently for the period 2010-14), through which municipalities commit themselves to implementing investment projects. Financing for these PIC investments is mobilized from CPSCL loans to municipalities, central Government subsidies (managed on behalf of the center by CPSCL) and own-source municipal revenues (with each of the three financing sources contributing about 1/3 of the total cost of the investment, except in the case of economic or commercial investments, for which no capital grants are provided). Central Government capital grants (effectively "hidden" inter-governmental fiscal transfers) thus account for about a third of municipal investment expenditures. The Table below summarizes the funding sources of the ongoing and previous four PICs.

Table 2: PIC Financing Plans from 1997 - 2019 in TND million

Sources of funding	1997-2001		2002-2006		2007-2010		2011-2014		2015-2019	
	TND mill.	%	TND mill.	%	TND mill.	%	TND mill.	%	TND mill.	%
OSR	253.5	29.5	130.8	18.8	87.6	16	166.7	20	193	16.1
CPSCL Loans	276.5	32.2	221.8	31.8	205.2	37	296.6	35	389	32.4
Capital Grants	158.0	18.4	177.2	25.4	197.2	36	270.9	32	305	25.4
Exceptional Grants	62.7	7.3	119.4	17.1	46.7	8	65.2	8	225	18.7
Others	109.2	12.7	47.9	6.9	14.7	3	44.3	5	87	7.2
Total	859.9	100	697.1	100	551.4	100	843.7	100	1200	100

17. **The Tunisian municipal sector has developed over the last decade. However, its institutional performance is still at a relatively early stage of development and needs to be reinforced**. Despite capital investments to support basic infrastructure delivery in urban areas, access to and quality of municipal services are far from sustainable. Municipal service delivery is deteriorating in most cities and particularly in lagging regions with significant impacts on quality of life, urban environment, public health, as well as on key economic activities such as tourism. Both a recent cross-sectoral scorecard undertaken on public services and a pilot municipal opinion survey undertaken in Tunisia showed widespread dissatisfaction with service delivery by municipalities and exceptionally limited engagement of citizens with their municipality.

18. **The new Constitution includes clear commitments to decentralization, local governance, and empowered LGs.** The provisions of the new Constitution create the framework for fully devolved and empowered LGs with autonomy for executing their mandates of providing local services according to transparent principles of participation by, and accountability to, their electorate. To this end, the Constitution lays down the mandate for LGs to achieve the following: (i) financial and administrative autonomy; (ii) participatory local democracy and open election of municipal representatives; (iii) formal assignment of functions according to principles of subsidiarity; (iv) own source revenues and transparent, objective and predictable systems of inter-governmental fiscal transfers, including consideration of issues addressing equity, equalization and national policy priorities; (v) governance structures that ensure participatory governance and accountability of municipalities to electorates in decision-making and program implementation; (vi) inter-municipal cooperation in metropolitan areas; and (vii) restructuring of the "*tutelle*" system to play an ex-post rather than an ex-ante oversight role. These constitutional principles and provisions are to be translated into a fundamental law ("*loi organique des collectivités territoriales*").

19. **In parallel with a new institutional framework, the Government is reforming the capital grant system.** The Government has recognized that, while it will be necessary to revise or replace the organic law and other related laws currently governing LGs, restructuring the capital grants system will offer the opportunity to introduce major changes that can immediately alter the landscape to more effectively address the Constitutional requirements, and provide for participatory governance at the local level. The reform of the capital grant system aims at addressing the following shortcomings:

- **Grant allocation system is not transparent.** The complexity of the inter-relationship between accessing grants, utilizing loans and providing counterpart funding, combined with the centralized system of determining eligibility for the grant funds is considered opaque and potentially inequitable. The system operates through procedures that are not perceived as transparent, objective and measurable, and are not predictable in a manner that facilitates consultation and effective planning.

- **Grant access procedures have led to financial stress due to the linkage between grant access and counterpart funding requirements.** Under the current provisions, the stipulated ratios between counterpart funding and grants have placed nearly half of all municipalities in situations of fiscal stress, where they have been required to borrow at levels they are now unable to service. Currently, 128 municipalities -nearly 50 percent- are unable to make payments and are technically in default. Reforms to the current PIC system, separating grant access from loans, will be essential to allow municipalities to continue undertaking investments in local services, while they formulate and initiate plans to redress their financial exposure.

- **The fiscal system undermines accountability between municipalities and their citizens.** The opaque allocation criteria, combined with the ex-ante control by the center on decisions regarding grant allocations, essentially break accountability linkages between municipal councils and their citizens. Councils are unable to plan since allocations are unpredictable. In addition, councils are effectively unable to consult with citizens since the decision on investments is taken at the center without consultation with municipalities. Consequently, final decision on investment selection is not with the municipalities, fundamentally weakening the potential of municipalities to practice participatory governance and establish sound social contracts with their citizens. The breakdown in accountability has had consequences that bear on the economic benefits of investments undertaken, the responsiveness of investments to citizens' priorities, the sustainability of these investments, and the willingness of citizens to respond to local revenue demands.

- **The fiscal framework and grant allocation procedures have disproportionately favored well-endowed municipalities.** Since access to the grant is conditioned on the amount of counterpart funds the municipality is able to generate, and borrowing is the only means of leveraging additional counterpart funds, distortions in allocations have increasingly prevailed. Only the stronger LGs have been able to provide the required co-financing, and consequently they have gained access to a disproportionate share of the grant funds, while the less well-endowed LGs with the greatest service deficits are being largely crowded out of the grant allocation system.

- **Lack of incentives and weak capacity for municipalities to perform.** The weak accountability relationship between municipalities and their citizens serves to limit incentives for the LGs to perform effectively, undermining their capacity across a broad range of functional responsibilities from planning and budgeting to Operations and Maintenance (O&M) of their assets. In this context, capacity support measures generally have limited impact. International experience strongly suggests that capacity-building support is far more effective when it is demand-driven.

- **Absence of LG performance and results monitoring systems.** Although under the current grant system, the Government maintains rigorous oversight of decisions on specific project investments by LGs, there is no system for converting and maintaining the data that such oversight offers. The project-by-project approach adopted so far does not provide broader data on institutional performance across any other parameters than project expenditure and rate of implementation. As a consequence, the Government does not have a comprehensive assessment of LG activities and performance. There is an urgent need to establish a performance assessment program that objectively measures, on a regular and timely basis, how municipalities are operating against a set of key indicators, and complement it with an information management system capable of providing the Government, and the general public, with this sort of information, both as something that should be required in its own right, as well as to support a data-based approach to local Government policy-making.

20. **The Government is committed to strengthening a participatory approach to local governance.** In response to the new Constitution which stresses the importance of participatory democracy, and in

light of the weaknesses identified in the existing system, the Government is undertaking major reforms to LG functioning, which can be introduced relatively quickly and with immediate impact, with the objective of addressing issues of participatory democracy; beginning the process of restructuring the *"tutelle"* system in favor of strengthening the independence and accountability of municipalities to better perform their essential functions; and enabling LGs to deliver local services more efficiently and effectively in response to citizens' identified priorities.

21. **The Government has recognized that reforming the PIC process offers new opportunities** to: (i) address, in the short term, key elements of the decentralization and participatory democracy agenda of the new Constitution that would have significant impact and that lend themselves to immediate initiatives while the broader and longer-term aspects are being formulated; and (ii) concurrently focus on critical municipal service delivery and investment priorities. The Government has also recognized, after more than 20 years of operation, that the effects of the existing PIC system as governed by Decree 97-1135 have resulted in perverse outcomes inconsistent with the original objectives of the grant, and not aligned with the decentralization policy reflected in the new Constitution.

22. **Key elements of Reform.** In response to these challenges, the Government intends to: (i) transfer decision-making authority on the selection of investments in local services to municipalities and their communities, through a process where municipalities will engage with and be accountable to their electorates; and (ii) underpin this with a capacity support system targeting core areas of municipal performance that is demand-driven and delivered on-the-job, and on a just-in-time basis. Key elements of the reform include:

- **Reforming the capital grant system** into an unconditional grant providing full discretion to the municipal council in deciding its utilization for meeting local service delivery and investment priorities. The grant system would operate through two steps, one subject to the municipality meeting basic minimum mandatory conditions (MMCs), the other rewarding municipalities according to their level of performance as determined by annual and independent performance assessments against pre-determined criteria.

- **Replacing the municipal investment ex-ante review** and approval system with the annual ex-post performance assessment of LGs.

- **Decoupling access to unconditional grants** from the compulsory requirement to borrow.

- **Introducing a formula-based grant allocation system** that comprises objective, measurable criteria which assure a transparent process, and that allow for predictability of resource flows for the municipalities.

- **Informing municipalities at the beginning of the PIC cycle** of the indicative five-year grant envelopes that they could potentially access, in order to strengthen their ability to plan more strategically and efficiently and on a more credible consultative and accountable basis with their citizens.

- **Replacing a project-by-project approach to funding Government priorities** (currently upgrading service deficiencies in disadvantaged neighborhoods) by introducing a system of conditional grants, whereby priority policies of Government that are best managed by the municipalities can be addressed on a transparent and systematic basis.

- **Introducing a capacity-building system** that enables municipalities to upgrade their performance in key targeted areas.

23. **The transition from a centralized to a decentralized system will take some time**, as laws will need to be realigned with the Constitution (there are a number of laws governing the institutional and fiscal operation of LGs that will require revision or replacement). Reforming the *"tutelle"* structure will be central to achieving a successful transition, as the existing system sublimates all facets of LG authority and decision-making to central and intermediate tiers of Government, as well as fostering dependency on deconcentrated arms of central agencies for various elements of service delivery. As a consequence, municipalities have limited capacity to exercise their essential functions effectively, severely undermining accountability and trust between elected municipal officials and their communities. Consequently, the challenges, which will take time to address, will be to: (a) reorient the central agencies to new roles in which they monitor performance; introduce changes in practices, regulations and laws in response to changing needs; develop support systems in response to demand; and respond selectively when critical intervention is required; (b) build national systems (for example fiduciary systems) that provide a framework for efficient, well-functioning and accountable public sector entities; and (c) create the enabling environment and support arrangements for LGs to operate effectively, improving local service delivery and encouraging active participation of their citizens. Concurrently, the high expectations for improvements to local service delivery are likely to increase.

24. In seeking to meet these challenges, reform initiatives are likely to encounter resistance from the *central administrations*, and therefore it will be important to introduce a process of change that: (a) recognizes the incremental nature of such fundamental shifts in policy, institutional responsibilities and operational procedures: (b) is nonetheless sufficiently strategic and comprehensive for the changes to achieve outcomes that have impacts in key, selected areas of the system; and (c) will be sufficiently robust to address the concerns of the *tutelle* system.

C. Relationship to the CAS/CPS and Rationale for Use of Instrument

25. **The proposed Urban Development and Local Governance Operation is consistent with the World Bank's Interim Strategy Note** (ISN) for 2013-14 (Report 67692-TN). The ISN spells out a set of three broad areas for Bank engagement and, within those areas, a number of Driving Objectives that the Bank will pursue. The proposed operation is fully aligned with the ISN's second area of engagement: promoting social and economic inclusion. Within this second area, the operation addresses Driving Objective 5, improving access to basic services for under-served communities. About half a million people, or eight percent of the urban population living in disadvantaged neighborhoods, are targeted through the proposed program. The proposed operation is also in line with the ISN's third area of engagement: strengthening governance through voice, transparency and accountability. The operation's focus on local governance institutions, decentralization, and significantly strengthening participatory democracy at LG level directly supports this.

26. **The World Bank has a long history of engaging with the Government of Tunisia** in the municipal development sector, addressing issues such as low access to LG infrastructure and basic services, an absence of training support for LGs, and limitations in access to LG finance. The previous three Bank-funded municipal development projects in Tunisia have been successful but limited attention was given to institutional development and LG accountability. The mostly "infrastructure" approach is no longer sustainable as decentralization, empowering LGs and local governance emerged as top national priorities. Since the January Revolution and particularly through the ongoing Tunisia Urban Technical Assistance Program, the Bank has developed a good record of engagement with decentralization and Local Government issues and has established ongoing dialogues with both Central and Local Governments.

27. **Rationale for use of the Program-for-Results (PforR) instrument**. The PforR has been identified as the most appropriate lending instrument to support the Tunisia Five-year Municipal Investment Program based on the following considerations:

- **Improving the efficiency of the Government expenditures in support of municipal investment.** The PforR instrument offers more opportunities to focus on improving the Government resources allocation system, its efficiency, and responsiveness to citizens' priorities, as well as LG performance versus a purely "infrastructure delivery" approach. Hence, it will help reforming the existing local Government fiscal architecture to conform to the provisions of the new Constitution regarding decentralization and participatory democracy.

- **Using program systems and procedures.** The PforR instrument will contribute to strengthening the program system for planning and implementation of municipal infrastructure sub-projects, social and environmental systems, fiduciary control, monitoring, and evaluation and management which will result in improved value for money in municipal investments. A core principle of the reforms to the grant system is that all the functions and mechanics for operating the reforms follow (and improve and integrate) Government systems and procedures regarding the operation of the grants at the central and local levels, as well as associated fiduciary practices.

- **Results orientation**. The instrument will promote results orientation of the overall program by establishing clear links between Bank disbursements and delivery of results.

- **Leverage.** Given that the Bank's own contribution is likely to provide about 82 percent of overall Government program financing, the PforR instrument will help support system changes across the program by leveraging the actions contained in the Program Action Plan (PAP), Results Indicators (RIs) and Disbursement Linked Indicators (DLIs) to reward positive responses on needed improvements.

28. **The Program resonates with the Bank's overall framework for engagement in the MENA region**. The operation seeks to: (i) strengthen governance, in general, and local governance, in particular, by enhancing the functions, financing and capacities of LGs, through the proposed reform to enhance the transparency and efficiency of the existing transfers system, LG accountability and by strengthening citizens' engagement; and (ii) increase the inclusiveness of local service delivery in Tunisia by strengthening LG performance and providing municipalities with the resources needed to finance the upgrading of informal and disadvantaged neighborhoods, particularly in lagging regions. As such, the Program directly addresses two of the four main pillars of the Bank's MENA Regional Strategy.

29. **The Program is also designed to advance the World Bank Group goals of eradicating extreme poverty and boosting shared prosperity.** The 2011 Revolution and associated civil strife were driven in part by the exclusion and inequality of opportunity for many Tunisians. The Government of Tunisia recognizes the importance of boosting shared prosperity and ensuring the wellbeing of all Tunisians. Although official estimates of aggregate extreme poverty in Tunisia are low (approximately one percent of the population in 2010), rates of poverty vary considerably from one percent in Tunis to 13 percent in the Middle West region of Tunisia. The Program will strengthen the capability of all LGs to sustainably provide municipal infrastructure and services to help improve the quality of life of Tunisians living in urban areas, and introduce mechanisms for targeting poor Tunisians, including poor women and youth. Two measures introduced through the Program are specifically designed to this end: the conditional transfers for municipal infrastructure investments in disadvantaged neighborhoods, and the equalization dimensions that will be introduced to the inter-governmental fiscal transfer framework. In addition to the long term growth enhancement associated with improved access to infrastructure and services, the Program is designed to increase public investment and create jobs – namely public works jobs – that could help increase income and improve the livelihoods of the poor in the short term.

II. PROGRAM DESCRIPTION

A. Program Scope

A.1 Government Program: Urban Development and Local Governance Program (UDLGP)

30. The Government program consists of delivering municipal infrastructure services in an accountable and responsive manner through a combination of grants, own source revenues of municipalities, loans, as well as institutional strengthening of 264 municipalities for the period 2014-2019. Through this program, the Government intends to shift from a purely "infrastructure delivery" approach to one that focuses on LG performance and accountability. To this end, the Government's program aims at: (i) strengthening LG institutional capabilities to deliver municipal services while transforming their relationship with their citizens through measures that are designed to foster participation, transparency, and accountability; and (ii) improving the municipal infrastructure service delivery to disadvantaged neighborhoods. The program is designed to build on existing LG strengths, while phasing in the changes that are designed to introduce fundamental shifts in critical, selected areas of LG institutional performance and governance that will enhance quality (through greater citizen consultation), accountability (through enhanced access to information on LG performance and grievance redress mechanisms), sustainability (through greater focus on asset management and local revenue generation), and management (through better financial accounting and reporting, financial performance improvement planning and debt management, as well as investment preparation, implementation and monitoring). In order to assure that the phasing, while ambitious, is workable, the program does not envisage near-term changes to the modest functional mandate currently assigned LGs, and does not propose to significantly expand investment levels until the platform of proposed reforms has been put in place, tested and made operational.

31. In this context, the reform of the capital grants and municipal investment planning framework forms the main strategic actions undertaken by the Government towards the implementation of its decentralization agenda anchored in the new Constitution. This grant system which had operated under an ex-ante system of controls is being restructured through the replacement of Decree 97-1135 with a new Decree governing the system of capital grants to LG. The provisions to the new Decree have been finalized by the Government, shared with the Bank, and are in the process of being formally adopted by the Government. Under the new Decree, the Government intends to improve the efficiency of state financial support to municipal investment, make the allocation of capital grants more transparent and predictable, strengthen the decision-making power of LG on their investment funding, and progressively introduce a performance based capital grant system. Along with introduction of the new Decree, the Government has also issued a Ministerial Circular to introduce participatory municipal investment planning and budget systems, hence promoting citizen engagement in identifying investment needs and priorities. Under the same reform, the Government will progressively introduce an independent assessment to measure the performance of LGs in line with the new Decree.

32. An assessment system, in addition to serving as a tool for monitoring LGs' ability to undertake key functions efficiently, has proven to be a very effective means of incentivizing LGs to strengthen their institutional performance, where access to grant funds is linked to results. The areas covered under the performance assessment will include governance, sustainability and management and the results of this assessment will be used to adjust the capital grant allocation starting the third year of the program

33. The Government program consists of three sub-programs, namely:

- Subprogram 1: Municipal infrastructure delivery.

- Subprogram 2: Improving access to municipal infrastructure in disadvantaged neighborhoods.
- Subprogram 3: Capacity support for improved LG institutional development and accountability.

Subprogram 1: Municipal Infrastructure Delivery (US$591 million)

34. Consistent with past practices under the PIC, the subprogram involves the preparation of five-year investment plans for each LG to deliver municipal infrastructure. Activities under the subprogram includes consultancy services (including feasibility and engineering studies, and support to implementation services) and civil works directly linked to LG core mandates such as roads and paving, construction, rehabilitation and upgrading, street lighting, sewerage extension/connection to public network, storm water drainage, solid waste collection, parks and some recreation facilities, markets, and other environmental improvements. An important modification to the prior system of PICs is the introduction of a programmatic approach to the five-year plans that provides for annual updates and revisions as local circumstances dictate.

35. The financing framework for the activities under this subprogram includes three sources of finance: (i) LG contribution; (ii) capital grants from central Government; and (iii) investment loans provided by the CPSCL. These sources of finance are discussed in the following paragraphs.

36. *Capital Block Grants for Municipal Infrastructure Delivery (US$203 million)*: LGs will receive capital grants from the Central Government to support priority investments in urban infrastructure that have been validated through a participatory planning approach and reflected in the LG municipal five-year (PIC) and annual investment plans.

37. The use of capital grants for municipal infrastructure delivery is determined solely at the discretion of each LG (without any ex ante control), subject to being used for municipal infrastructure investments that fall within the mandates of the LGs. It will be allocated on the basis of a formula and the use of these resources is determined solely at the discretion of each LG (without any ex ante controls), reflected in their annual investment plan and subject to their being used for municipal infrastructure investments that fall within the mandates of the LGs.

38. The total capital block grants for municipal infrastructure amount to US$5.7 per capita/year. Key investment activities of the program are presented in Annex 1 and include road construction, rehabilitation and upgrading, street lighting, urban drainage/sewerage and other environmental improvements, solid waste collection and street cleaning, parks and some recreation facilities, markets and slaughterhouses.

39. *Local Government Contribution (US$129 million):* In parallel with the above capital grants, the Government's 2014-2019 PIC envisages LG contributions to increasing levels of investment in municipal infrastructure. The Government recognizes that reforming the own source revenue system will take time as it involves major policy changes, and is therefore focusing on opportunities for improving local revenue collection rates within existing tax and fee regimes.

40. *Municipal Investment Loans (US$259 million):* In addition, LGs capable to borrow will have access to the CPSCL credit line as a potential funding source to implement their Municipal Investment Plans (PIC). The Loans from the CPSCL serve to maximize leverage of resources available to LGs for investing in municipal infrastructure. In parallel, the Government is introducing reforms under the Decree and in the CPSCL lending guidelines in order to establish a stable balance between maximizing borrowings by the LGs and maintaining their financial viability.

Subprogram 2: Improving access to municipal infrastructure in disadvantaged neighborhoods (US$150 million)

41. Under this subprogram, the Government provides conditional grants directed towards investments that represent national policy priorities (in this case, for the new PIC period, to improve access to municipal services in disadvantaged neighborhoods).

42. Activities under the subprogram includes consultancy services (including feasibility and engineering studies, and support to implementation services) and civil works for the provision of infrastructure such as roads and paving, street lighting, sewerage extension/connection to public network, and storm water drainage in selected disadvantaged neighborhoods located in 144 LGs.

43. The conditional grant allocation over the program period amounts to US$150 million or an average of about US$1 million per LG which represents around US$284/beneficiary (US$1,420/household).

Subprogram 3: Capacity support for improved LG institutional development and accountability (US$10 million)

44. The Government's program upgrades the system of capacity support for LGs in order for them to achieve improved institutional performance targets. The capacity support program would contribute to the LGs' ability to achieve the standards required under the performance assessment system to help them access their full entitlement of capital grants. Under this subprogram, LGs receive capacity development and technical support to prepare and implement their plans via training programs offered by the Decentralization Support and Training Center (*Centre de Formation et d'appui à la Décentralisation, CFAD*) and technical assistance from regional offices of the CPSCL and line agencies of central Government, as well as through local consultancy services.

45. An allocation of US$10 million will be committed through the national budget for the financing of this subprogram. Half of this amount is earmarked for technical assistance through framework contracts to be signed at the level of each regional office of the CPSCL for the provision of on demand technical assistance to LGs. This program being demand-based, the Government envisages the commitment of additional resources if assessed necessary during the Program's Mid-Term Review.

A.2 Program for Results Financing (Program)

46. **Duration**. The Program implementation period is from 2014 to 2019.

47. **Geographic scope.** The Program will finance activities in the same geographical areas (the Program Area) covered by the Government sub-programs: all 264 municipalities (LGs), plus any new ones that may be constituted during Program implementation.

48. **Activities to be supported by the Program.** Based on the need identified during the preparation of the Government program and for increased selectivity of Bank support, the Program encompasses three primary activities: (a) capital block grants for municipal infrastructure delivery reflecting citizens' priorities; (b) targeted capital grant for improving access to municipal infrastructure in disadvantaged neighborhoods; and (c) capacity support for improved LG institutional development.

49. Consistent with the Government's approach of phasing in its decentralization agenda, the Program has been built around those elements of the Government's program that offer the opportunity to have the greatest impact in the near term. In this context, the Government, in discussion with the Bank, has made

the strategic decision to focus on the capital grant as the most effective means of introducing the desired LG institutional reforms. Both the Government and the Bank recognize that the loan and OSR funding instruments are important elements of the LG infrastructure investment financing framework. In the case of the CPSCL (the loan program), an in-depth assessment is being undertaken, in parallel with the PforR, with assistance from other agencies such as the French Development Agency (AFD) and the European Investment Bank (EIB). The assessment is designed to determine the status of the CPSCL as a financial intermediary, as well as review its operating systems and its business plan, and this may well involve major institutional restructuring which will take time. Similarly, reforming the OSR system will require fundamental policy and procedural changes which the Government has concluded should be made at a later date. The PforR recognizes the linkages of the grant system to both the loans and the OSRs, and takes account of them. Specifically, improvements in OSR management and collection are incorporated into the grant's performance assessment system, and the rigor with which loans to LGs are made is to be strengthened through the introduction of the requirement of the preparation of financial performance improvement plans by the LGs, which will form part of the LG performance assessment criteria.

50. Taking these considerations into account, the Government and the Bank have agreed to limit the scope of the Program to supporting the capital grant reforms and related capacity-building assistance. Underlying this approach is the recognition that the reform agenda supported under the Program has to be one of strategic incrementalism in which the first steps are to: (i) begin the process of setting up a culture of inter-governmental fiscal transfers based not on central discretion but formulae and predictability; (ii) establish access to information that requires (and enables) LGs to report back to citizens and the central Government on the receipt and expenditure of these transfers on a regular and timely basis; and (iii) builds systems and capacity. Only after this culture and systems have set in will a significant shift in service delivery improvements occur, creating the opportunity for expanding the functional mandate of the LGs and scaling up investment levels.

51. As a consequence of the decision on the scope of the Program, the reforms to the LG capital grant system, the responsibility for implementing them, their relationship to achieving improved performance of the LGs, and impacting results at the local level, were placed at the core of the Program design. Specifically, it is Decree 97-1135 that: (i) provides the framework for translating the laws into the regulation; (ii) governs how the capital grant funds are allocated between LGs; (iii) determines how these funds are used by the LGs; (iv) establishes the conditions for accessing the funds; and (v) mandates that these regulatory functions are the responsibility of the CPSCL. Consequently, although the Program is aimed at improving the operation of LGs and enhancing the development of effective social contracts between LGs and their citizens, the primary instrument for achieving this is the structure of the new Decree. Hence the focus of the Program (and many of the DLIs) is on the introduction and operationalization of the Decree. If the reforms under the Decree are well-constructed, they then offer the most effective form of incentivizing the Government to ensure that LG performance targets are met by enforcing the provisions of the Decree. Since funds to the Government under the Program are determined by these targets being met, while each LG is incentivized to achieve its individual performance targets since the Decree (as a legal instrument) mandates this in order for the LG to access its grant entitlement as funded by the Government's annual budget allocation for this purpose. The design of a well-crafted Decree is also central to tackling the relationship of the "*tutelle*" to the effective functioning of the reforms. The Decree is considered to be the most resilient vehicle for embedding the reforms as it carries with it the force of law, and it has been carefully designed to fit within the existing legal system. It comprises all the elements of the first phase of the decentralization reforms that would make it consistent with envisaged future changes to the organic law for local Government.

52. The Table below presents the Program (gray shaded cells) vis-à-vis the Government program.

Table 3: Government's program and PforR Program Scope

<table>
<tr><td>Subprogram 1
Municipal infrastructure delivery

TND 887 million (US$591 million)</td><td>Subprogram 2
Improving access to municipal infrastructure in disadvantaged neighborhoods

TND 225 million (US$150 million)</td><td>Subprogram 3
Capacity support for improved LG institutional development and accountability

TND 15 million (US$10 million)</td></tr>
<tr><td>Capital Block Grants
TND 305 million (US$203 million)
Formula-based grant allocation to LGs subject to their meeting annual Minimum Mandatory Conditions (MMCs) and achieving satisfactory annual performance scores.</td><td rowspan="3">Conditional Capital Grants
TND 225 million (US$150 million)
Grant allocation to LGs for specified investments in line with national priorities (currently for local infrastructure in disadvantaged neighborhoods), subject to their meeting a Minimum Mandatory Condition (MMC) grant access requirement.</td><td rowspan="3">Capacity-building and technical support TND 15 million (US$10 million)
Demand-based capacity support to be provided to LGs on a just-in-time basis.</td></tr>
<tr><td>LG Contribution
TND 193 million (estimate)
LGs Contribution to the investments from their net savings.</td></tr>
<tr><td>Municipal investment loans
TND 389 million (estimate)
Investment loans to LGs from CPSCL.</td></tr>
</table>

53. The following presents the specific objectives and core elements of the three areas supported by the Program.

A. *Capital Block Grants for Municipal Infrastructure*

54. The capital block grants would be performance-based to incentivize LGs to achieve improved standards of institutional performance in key areas of their municipal functions. The target would be for 60 percent of LGs to achieve scores of 70 percent or more on their evaluation for the fifth year of the Program. To achieve the targeted outcomes, the Program provides resources under the capital block grant for investments in local infrastructure services, with funding levels modulated by each LG's ability to meet annual performance standards applicable to unconditional grants as measured by annual Minimum Mandatory Conditions (MMCs) and Performance Assessments (PAs) undertaken according to agreed criteria. The annual performance standards include implementation of participatory planning and transparency initiatives.

55. Under the Program, 264 municipalities will receive capital block grants from the CPSCL (on behalf of the State) to support priority investments in urban infrastructure that have been identified and reflected in their participatory five-year and annual municipal investment plans. The municipalities will be responsible for planning and implementing sub-projects financed with capital block grant funds, and grant funds will be reflected in the revenues and expenditures of their annual budgets.

56. Capital block grants will be allocated to the municipalities according to a transparent and predictable formula. These allocations are weighted by LG population and fiscal potential (80/20), subject to the application of an adjustment factor to ensure that each municipality receive at least the equivalent of the envelope received during the previous PIC. These allocations provide an average annual allocation of US$29 per capita over the period of the Program, plus 12.5 percent compared to the current PIC.

57. These allocations are for planning purposes and the actual annual disbursement of funds will be made on the basis of: (i) meeting the MMCs; and (ii) each city's performance to be measured against a set of criteria. Details regarding MMCs and PAs are included in Annex 1.

B. *Conditional Capital Grants for Improving Access to Municipal Infrastructure in Disadvantaged Neighborhoods*

58. This conditional capital grant represents a vehicle for the Government to address policy priorities. Currently, Government priority is focused on upgrading service levels in disadvantaged neighborhoods. A total of TDN 225 million has been allocated under the conditional grant for the PIC 2014-2019 period for this purpose. Due to resource constraints and the uneven distribution of disadvantaged neighborhoods across LGs in the country, a regional consultation process (involving elected officials from the National Constituent Assembly, representatives from regional and local Governments, civil society, deconcentrated agencies) was undertaken to pre-identify neighborhoods and municipalities which would qualify to receive these grant funds during the CY2014-2019 cycle.

59. The application of the performance system to the conditional grant is limited to the MMCs on a one-time basis for the year when the construction of the approved upgrading plans is projected to commence.

60. The Program will bring in innovations compared to past upgrading programs, particularly for: (i) full ownership and responsibility of LGs in preparing and implementing the related investments as part of their municipal investment programs; (ii) deep consultative and participatory approach for neighborhoods identification/prioritization and for neighborhood identification of priority investment needs; (iii) highly subsidized financing scheme aligned with the financial capacity of LGs to avoid existing additional municipal finance stress to access capital grants; and (iv) provision of just-in-time support to LGs to implement sub-projects and develop capacity from the implementation.

C. *Capacity Support for Improved LG Institutional Development and Accountability*

61. The capacity support would contribute to the LGs' ability to achieve the standards required under the performance assessment system in order for them to access their full entitlement to the capital grants. It will focus on the key support required to assist municipalities to achieve MMCs and performance criteria, and thus contribute to the achievement of the Program Development Objective.

62. Given the heterogeneous demand from municipalities, capacity and technical support will be provided based on an annual LG Capacity Development Plan (LGCDP) which will be prepared by each LG to address its needs. A preliminary capacity needs assessment was carried out during Program preparation and four broad areas were identified as requiring capacity-building support at the city level: (i) municipal investment prioritization and planning, including citizen participation and oversight; (ii) financial management including own source revenue enhancement; (iii) project quality, including procurement and environmental and social management; and (iv) asset management systems and mechanisms for operations and maintenance. The LGCDPs will be supported through formal training provided by CFAD, and will include targeted courses that will be developed and introduced by CFAD as the need presents itself over the course of Program implementation. In addition the LGCDPs will be supported by a system of "just-in-time" technical assistance to assist the LGs in developing the capacity to handle those key functions that are considered core to the effective operation of sound local Government, and which will be central to the PA system. These LGCDPs will include the LG's estimates of its needs for such technical assistance, but the "just-in-time" system will also be designed to respond quickly to demands as they arise, even if not anticipated in the LG's LGCDP. The just-in-time program will be managed by the regional offices of the CPSCL, supported by consultancy contracts with firms that will be structured around the principle of providing expertise as needed.

Box 2: Lessons Learned from Previous LG Development Projects in Tunisia

Firstly, efforts to increase organizational efficiency and reform formal institutions are necessary but insufficient for strengthening LG capabilities. Previous LG development projects in Tunisia introduced tools and other inputs for improving organizational efficiency, but efforts to improve institutional efficiency were limited. This program will focus on improving institutional efficiency by increasing LG responsibilities to allow them to learn by doing, and offering demand-driven, better tailored and more accessible support to LGs. Furthermore, the project will enhance monitoring and evaluation systems to improve learning. The stronger focus on effective capacity-building is signaled in part through the allocation of a substantially larger share of the loan to institutional development activities.

Secondly, improvements in the provision of LG infrastructure and services may be suboptimal if citizens lack the knowledge or means for influencing LG decision-making. The existing PIC process is an approach that has contributed to substantial improvements in access to LG infrastructure and services in Tunisia; however, under the previous political regime, it lacked effective means for engaging citizens in LG planning and governance. This exclusion could help explain citizen dissatisfaction with LG performance in Tunisia. This Program will introduce new tools to enable citizens to engage in local decision-making and monitor project outcomes.

Thirdly, institutional reforms of this nature are complex medium- to long-term endeavors which require realism and flexibility. Previous LG development projects in Tunisia were ambitious in their scopes, timelines, and expected results. This ambition led to premature load-bearing and reduced the expected impact of certain interventions. The scope for reforms that could be undertaken through this Program remains large; but to maximize the likelihood that sustainable reforms will be accomplished, the Program has been designed to: (1) take a gradual and realistic approach to all facets of the Program including the timeline and expected impacts; and (2) balance addressing urgent needs of the people and Government of Tunisia with introducing reforms aimed at addressing systemic issues constraining LG performance.

63. The Program will also support the introduction of several initiatives that will focus on those central institutions and systems that have significant roles in the effective operation of LG in Tunisia, and which will strengthen the Government's decentralization, participatory governance and transparency agenda as established under the new Constitution. This will include support for: (i) the design and launch of a new

e-Portal (*Portail des Collectivités Locales*) which will prepare budget, procurement and audit information for all LGs, as well as the results of LG performance assessments accessible to the public (and, progressively, the e-Portal will also host LG information on Participatory Planning and Participatory Budgeting processes); (ii) the expansion of the Court of Auditors's (*Cour des Comptes*) annual LG financial auditing function to increase annual coverage so that by the end of the Program, 80 percent of LGs are being audited annually, with the intention of this being expanded to eventually ensure 100 percent coverage; (iii) the introduction and operationalization of the annual PA, to be undertaken by the Controller General of Public Services (*Contrôleur-General des Services Publics (CGSP))*; and (iv) the delivery of a series of nationwide workshops by CFAD with assistance from DGCPL and CPSCL to introduce and familiarize the LG system (LGs, relevant institutions and Government agencies, and the general public) with the Program and PA process. Table 4 summarizes the capacity-building arrangements under the Program.

Table 4: Capacity-Building Arrangements under the Program

Area of Support	Description	Supporting agencies	Timing
Formal LG Training	Formal training programs addressing the functioning of decentralization systems and the operational responsibilities of LGs, for both elected officials and staff;	CFAD	Formal system already operational
Technical Assistance to LGs	Program of on-the job, just-in-time assistance provided to LGs on a demand-driven basis. Designed around principle of "learning by doing" and structured to provide expertise in key areas of LG need (finance, technical/engineering; social/citizen participation/accountability; fiduciary)	Caisse with assistance of CFAD and DGCPL	Offers opportunity of quick impact and "early wins". Should be fully operational in time for start of 2015.
Targeted Initiatives to Strengthen LG System	• Systematization of LG financial auditing of LGs • Introduction and operationalization of Performance Assessment (PA) System • Introduction of E-Portal to improve access to information to enhance LG accountability to citizens, and to strengthen DGCPL oversight (M&E) • Nationwide workshops to introduce and familiarize LG system with Program and PA system • Targeted training for LGs (procurement, safeguards, other – as needed)	• Cour Des Comptes • CGSP or CGF • DGCPL • CFAD • CFAD	• 2015 • 2016 • 2015 • 2014 • 2015

Program beneficiaries

64. The primary beneficiaries are the 264 municipalities and their seven million urban citizens (or 2/3 of the country's total population). They will benefit from enhanced inter-governmental transfers and from demand-driven institutional and capacity development activities, which will strengthen delivery of municipal infrastructure and services efficiently and consistent with citizens' priorities. They will also benefit from initiatives to build knowledge and capacity of municipal council members and municipal staff on participatory governance initiatives which will underpin broader efforts to strengthen municipal

efficiency and build a social contract between citizens and LGs. The participation of local communities including, importantly, women and youth, in planning development activities managed by the municipality at the local level will ensure all groups' needs are addressed, further fostering citizens' engagement and contributing to long-term sustainability.

65. The secondary group of beneficiaries are people living in targeted underserviced/disadvantaged neighborhoods (more than 500,000 inhabitants in 229 neighborhoods). The main benefits will come from improved access to municipal services, overall improved municipal management and direct involvement of the population in setting investment priorities. Investment activities financed through project funds will benefit this entire target group either directly or indirectly, including through creation of temporary employment which is likely to benefit, in particular, youth.

Citizen Engagement

66. The civil unrest experienced by Tunisia reflected citizens' widespread discontent with a highly centralized Government out of touch with their needs and concerns. Tunisia's new Constitution supports a profound shift from this old system, promoting a decentralized system of local governance, and ensuring citizens' direct participation in public programs.

67. The adoption of participatory governance presents new challenges for Tunisian LGs which have traditionally had very limited engagement with residents and little, if any, experience with participatory methodologies. A municipal opinion survey conducted in 2014 in a mid-sized LG in the Tunis metro area illustrates the extent of LG-resident disconnect: just four percent of households report having received any communication from the LG in the past year; some 35 percent of households do not know who their LG Councilors are; over 64 percent of households think their Councilors do not work to represent residents' interests and priorities; and 38 percent of households report that they do not pay their local taxes. However, the survey also reveals citizens' interest and willingness to engage with their LG. Close to three quarters of households said they would like to receive more information from their LG; over half are interested in attending information sessions to learn more about their LG's planning and budgeting process; and 67 percent said they would be willing to pay slightly higher local taxes if they were sure this would result in improved service delivery.

68. Although LGs are eager to engage more effectively with their residents, they lack experience on how to do this and will need to introduce the new measures while public discontent and distrust remains high. The Program thus supports Tunisia in introducing a practical and feasible participatory planning and budgeting framework across all 264 LGs. The Program will provide guidance, training and mentoring for LGs by introducing a participatory planning approach which requires them to share their proposed annual capital investment plans with residents and secure validation for the plans in open public fora. Adoption of this approach will be part of the PA. The operationalization of an open-access e-Platform hosting all municipalities' budget, contracting, and public outreach information will also be supported by the Program to promote greater transparency and facilitate monitoring of progress.

Gender-Oriented Benefits

69. Tunisia's new Constitution of January, 2014, in the Chapter dealing with LGs, requires all local authorities to ensure the "broadest participation of citizens" in development programs. Elsewhere it commits the State to guaranteeing equality of opportunity for women and men and to working for parity of women and men in elected assemblies. These are important provisions and the Program will support several initiatives intended to encourage women's participation in, and benefit from, LG programs. Under the Program's new participatory budgeting initiative, which will be introduced at the municipal level, LGs will be incentivized to earmark a modest percentage of their annual capital investment grants

to support small infrastructure programs which will be proposed by municipal residents and resident civil society groups. While votes cast by residents will determine which proposals will receive funding each year, those which include provisions for women will receive extra weighting, and the annual PA will take into account the extent to which investment choices by LGs reflect gender considerations. This approach should, as has happened in other countries, provide strong incentives for residents to both engage in the participatory budgeting process with their LG, and to consider women's needs in their localities. It has also been demonstrated to foster greater responsiveness on the part of LG councils to their citizen's priorities. At a more macro level, the Program will also provide specific benefits for women through its support for the extension of core municipal services in the country's most disadvantaged neighborhoods. It is expected that a sizeable proportion of this support will finance new tracks of public lighting and sidewalks in these disadvantaged neighborhoods, two basic services which have been shown repeatedly to be given high priority by women.

Program financing

70. The total outlay of Program and the Government indicative allocations among the three Program elements are presented in the Table 5 below. The IBRD loan of US$300 million represent about 83percent of the total cost of the Program (US$363 million).

Table 5: Program Elements

	Amount (TND Million)	Amount (US$ Million)[6]
Capital Block Grants for Municipal Infrastructure Delivery	305	203
Conditional Capital Grants for improving municipal infrastructure in disadvantaged neighborhoods	225	150
Capacity support for improved LG institutional development	15	10
Total Program Financing	**545**	**363**

B. Program Development Objective

71. The objectives of the Program are: (i) to strengthen Local Governments' performance to deliver municipal infrastructure, and (ii) to improve access to services in targeted disadvantaged neighborhoods.

C. Program Key Results and Disbursement Linked Indicators

72. Progress towards the PDO will be measured through a set of simple and measurable indicators; most of them will be linked to disbursements. The Results Framework for the Program has three key results areas that are closely inter-related. Each results area is linked to DLIs, Program Actions and planned capacity support, as well as to monitoring, evaluation, and verification activities in the Program. This provides a coordinated incentive for LGs to improve their capacity to plan, prepare and implement municipal infrastructure delivery with a focus on poor neighborhoods. The Results Framework and monitoring arrangements are provided in Annex 2, while the DLIs are provided in Annex 3.

73. The proposed key Program results indicators are:

[6] Exchange rate: 1USD = 1.50 TND

- Percentage of LGs that achieve at least 70 percent score in their annual performance assessment. [7]

- People living in targeted disadvantaged areas benefiting from improved municipal infrastructure (disaggregated by gender).

74. The Disbursement Linked Indicators (DLIs) have been selected to reflect critical elements of performance required to achieve the PDO as well as the intermediate outcomes, as reflected in the results matrix in Annex 2. The DLIs are summarized in Table 6 below, and the complete DLI matrix is provided in Annex 3.

Table 6: Disbursement Linked Indicators

Disbursement Linked Indicator	**Estimated disbursement amounts (US$ million)**
DLI 1: The Borrower has replaced Decree No 97-1135 and restructured its capital grant system accordingly.	30
DLI 2: Timely communication to LGs of the indicative Capital Block Grants (CBGs) allocation and timely transfer of CBGs to eligible LGs by the Borrower.	20
DLI 3: Acceptable percentage of LGs have met the MMCs and received CBGs.	30
DLI 4: The Borrower has designed and implemented an independent LG performance assessment (PA) system and required percentage of LGs have met the threshold PA scores.	90
DLI 5: Required percentage of LGs have executed their Annual Investment Plans on schedule in terms of expenditures.	45
DLI 6: Required percentage of LGs have received capacity-building support in accordance with their annual capacity development plan.	25
DLI 7: Targeted number of people living in targeted disadvantaged neighborhoods have benefited from improved municipal infrastructure.	40
DLI 8: Transparency and access to information have been improved.	20
Total	**300**

75. The Program Results Framework and DLIs represent a consistent results chain across all levels of Government and create a complementary set of incentives necessary to achieve the PDO. At the Program level, each set of DLIs provides an essential complement to the others. For example, institutional strengthening is a critical requirement for both infrastructure delivery and sustainability, and must be supported by a transparent, predictable and equitable allocation of State financial support to LGs. The selection of specific DLIs reflects the assessment of critical challenges facing LGs and the Government which are considered to be essential to the achievement of Program results. Moreover, dedicated local management capacity is essential to effective local planning, investment quality and asset management, better mobilization of fiscal potential and efficient use of investment funding sources, while national oversight is essential to strengthening local accountability as measured through the annual evaluation and assessment process.

76. The disbursement amounts associated with the DLIs are weighted to reflect these mutually reinforcing relationships between transparent and predictable allocation of state financial support to LGs, informed and participatory municipal investment planning, improved local institutional performance and

[7] Performance areas include: governance, sustainability and management.

accountability, timely implementation of municipal investment plans, and access to fiscal transfer and LG performance information.

77. The definition of the DLIs, the verification protocols and the basis for the calculation of disbursements are provided in Annex 3.

III. PROGRAM IMPLEMENTATION

A. Institutional and Implementation Arrangements

78. Taking into account the fiscal nature of the reforms introduced under the Program, the Ministry of Economy and Finance (MoEF) is responsible for the Program and consequently the activities under the Program are financed directly by the MoEF through its annual budget. The MoEF will be responsible for Program implementation and for all transfer of funds under the Program. This will include ensuring that Program resources are budgeted for and disbursed within the Program expenditure framework according to existing state budget procedures.

79. An Inter-Ministerial Committee (IMC) was established on August 5, 2013, to oversee coordination of the Program, and is chaired by the Minister in charge of Local Governments within the Ministry of Interior (MoI)[8]. The IMC meets bi-annually (plus exceptionally as needed), providing strategic leadership and general direction for overall implementation of the Program. It is supported by the DGCPL, which will serve as the Secretariat to the IMC. The IMC is responsible for sectoral coordination and for providing strategic leadership and general direction for the overall implementation of the Program.

80. The CPSCL is mandated under the Decree and according to the Law no. 37 dated May 14, 1975, to administer the capital grant transfers to the LGs. The process of the Capital Grant transfers will be detailed in the Program Operations Manual. The CPSCL will be responsible for coordination of day-to-day implementation of the Program and will facilitate the timely completion of inter-dependent functions to be performed by the several supporting agencies. Its responsibilities and functions in this regard, as well as those of the supporting agencies and the LGs will be detailed in the Program Operations Manual.

81. The CPSCL will be directly responsible, through its regional offices, for the execution of the technical assistance (just-in-time support) activities of the capacity-building program (as described above).

82. As the agency designated to coordinate day to day Program implementation, the CPSCL will ensure adequate reporting through: (i) day-to-day monitoring of implementation progress of the Program; (ii) Program reporting, including the annual midyear report and Program Progress Report; and (iii) preparing the Program Financial Statements, compiling them from municipal financial reporting, as well as from the financial reporting of the other supporting agencies.

83. The other national entities who will have guiding and supporting roles in the Program include: the Court of Auditors (*Cour des Comptes*), especially for the annual program audits and the annual external audit of municipalities; the Public Procurement Oversight Committee (*Haute Instance de la Commande Publique, HICOP)* which provides overall technical guidance on public procurement and monitors the compliance of procurement standards and practices; the Market Monitoring Committee *(Comité de Suivi et d'Enquete sur les Marchés, COSEM)* which receives pleas relating to public procurement and takes

[8] Membership of the IMC includes representatives from the following ministries and Governmental agencies: (i) Interior, (iii) Economy and Finance, (iv) Regional Development, (v) CPSCL, (vi) CFAD, (FNVT) and (vii) ARRU.

follow up action; the Controller General of Public Services *(Contrôleur Général des Services Publics, CGSP)* or any designated independent entity acceptable to the Bank which will be in charge of the annual and independent PA of the LGs; and the National Authority for Fighting Corruption *(Instance Nationale de Lutte contre la Corruption*) which will be responsible for the investigation of complaints, if any, on fraud and corruption relating to the Program.

84. At the local level, LGs will plan and implement investments financed under the Program, building on the well-established systems and procedures developed during the last 20 years with support from the three previous Bank-funded Municipal Development Projects. As these LGs are the project owners for individual investment projects, funding from the grants will be reflected in the revenues and expenditures of the LG annual budgets. The LG will prepare the annual municipal investment plan for the Program, consolidated with the annual budget plan of the LG. The annual budget is discussed and approved by the municipal council and the annual municipal investment plan and the annual budget will be disclosed after adoption. The LG will be responsible for approval of feasibility studies and basic designs, detailed designs and cost estimates and procurement plans.

85. The LGs will ensure that their technical and administrative departments are adequately staffed and resourced and will outsource the supervision of their sub-project implementation to private or public entities when needed. Financial management, procurement and environmental and social management activities will be undertaken by LGs in accordance with enhanced Government procurement rules and procedures, including the preparation of: (i) annual investment plans; (ii) consultancy services terms of reference; (iii) feasibility studies, including necessary social and environmental impact assessments; (iv) detailed designs and cost estimates; (v) tender documents; and (vi) the annual procurement plans. LGs will also be responsible for: (i) all procurement actions including advertising, bid evaluation and award of contracts; (ii) contract administration and management; (iii) technical supervision; (iv) verification of contractor's claims for payment, and issuing payment instructions to the municipal treasury (*Receveur municipal)*; (v) monitoring and proper reporting of physical progress of investments; and (vi) ensuring assets are entered in the asset register of the LG on commissioning.

86. Municipalities require a wide range of expertise to successfully carry out their mandates. An analysis of staffing carried out as part of Program preparation reveals that most municipalities have the necessary staff, but all LGs are expected to have the necessary support from DGCPL, CFAD and CPSCL and consulting firms, as LGs that do not meet the minimum mandatory condition will not be able to access Program funds.

B. Results Monitoring and Evaluation

87. The Results Framework (Annex 2) provides the basis on which the CPSCL, in close coordination with LGs and supporting agencies, will appropriately measure and report on progress.

88. CPSCL will prepare Program progress reports annually, as outlined in the Results Monitoring and Evaluation framework. The report will include consolidated financial statements that will cover all Program activities, expenditures and sources of funds, implementation status, progress in achieving the DLIs, result indictors, and evidence of compliance with requirements of the Program Action Plan. The Program Operations Manual will include the format and details of reporting.

C. Disbursement Arrangements and Verification Protocols

89. Once satisfied with the comprehensiveness of the reporting, the CPSCL will present annually, by February 28, evidence of the DLI's achievement (covering the period of January 1 to December 31 of the previous year) to the Bank, who will verify, with support from an Independent Verification Agent (IVA)[9], the results by no later than May 31 each year using the Results Verification Report. When satisfied with the review of this report, the Bank will issue a notification to the Borrower confirming fulfillment of the Disbursement Conditions against these specific DLRs. Upon receipt of such notification, the Borrower will then submit a withdrawal application to the Bank.

90. The Government has informed the Bank that advances will be needed. Advances up to US$60 million or 20 percent of the total IBRD loan would be made by the Bank to MoEF. This, in the nature of a rolling advance, will be adjusted against the claim of disbursement against DLIs 5 and 7. The Bank requires that the Borrower refund any advances (or portion of advances) if the DLIs have not been met (or have been only partially met) by the Closing Date of the Program, promptly upon notice thereof by the Bank.

91. Additionally, a disbursement against DLI1 in the amount of US$30 million (or ten percent of the IBRD loan amount) will take place upon Program effectiveness for achievement of a Prior Result as the corresponding target is expected to be met prior to the date of the operation's legal agreement.

IV. ASSESSMENT SUMMARY

A. Technical (including Program economic evaluation)

Strategic Relevance

92. In response to the Revolution of 2011, Tunisia has sought to introduce policies that firmly ground voice and accountability into the governance structure of the country. To this end, the new, recently adopted constitution embeds decentralization as a cornerstone of its strategy to bring Governments closer to its citizens. This requires transformational changes to the operating framework of LGs, and the Program is designed to support key reforms necessary to restructure the institutional and fiscal framework to more effectively address the decentralization provisions contained in the Constitution. The reforms pose several challenges to the existing structures of LGs, most notably, in light of the greater municipal autonomy mandated in the Constitution, the need to: (i) strengthen the LGs to be better able to perform their essential functions of citizen consultation and accountable service delivery independently of central intervention; (ii) reform the existing oversight system (*"tutelle"*) from central Government controls, clearances and approvals for local investment decision-making, to one of central support, capacity strengthening and policy reform for local Governments to better undertake their mandates; and (iii) address several key provisions of current regulatory requirements in the operation of LGs, particularly regarding the fiscal architecture of inter-governmental transfers that have proven counter-productive and have fostered outcomes contrary to those intended by the policies in place.

93. **The Program design has high strategic relevance for Tunisia's development.** It is calibrated to introduce the reforms in a manner: (i) recognizing that the transition to an effectively functioning decentralization system of fully-devolved LGs will take time; (ii) that builds on existing systems, taking advantage of existing strengths; and (iii) that introduces changes to the fiscal architecture and regulatory framework necessary to directly translate the Constitutional mandate into practice in areas that offer prospects for early wins and establish the core elements of viable and accountable local governance. The

[9] The IVA's role is to provide independent confirmation of the results reported by the LG and the CPSCL to the Bank. This includes verification of performance of the Program with regard to the Program DLIs, the extent to which the Program DLIs have been achieved, as well as the preparation of a Program Results Verification Report.

restructuring therefore is carefully sequenced to focus on those actions that on the one hand will have transformative consequences and introduce sustainable systems and practices, while on the other hand are phased in accordance with graduated reforms that are practical and can be implemented in the short term to have an immediate impact on addressing key provisions under the Constitution.

94. The Program will therefore operate within the existing fiscal architecture by restructuring the existing capital grant system for transferring resources to municipalities from a system that is regulated by centrally determined and opaque allocation procedures and investment priorities, into a window regulated by a system of resource transfers made according to: (i) a formula-based capital grant system for uses determined fully at the discretion of the LGs; and (ii) a conditional grant system managed by the LGs but for investment purposes deemed to be national policy priorities. The formula-based grant system addresses issues of allocative equity, objectivity and transparency, while also introducing incentives to perform better along key parameters essential to enhancing accountability of the LGs to their citizens and strengthening their planning, fiduciary and operating capabilities.

Technical Soundness

95. The Program is technically sound, drawing on international best practice and integrating it with the specific circumstances of the Tunisian reform initiative. In particular, consistent with the Government's policy of phasing in its decentralization policy, the Program utilizes fiscal instruments to effectuate the initial round of reforms.

96. Specifically, the Program conforms to principles core to international experience in operating an effective fiscal decentralization framework, including: (i) linking the transfer of grant resources to improvements in LG institutional performance; and (ii) introducing reforms by restructuring the current LG grant window into two sub-windows, while building on the existing, well-established fiscal architecture for LG transfers and the well-capacitated institutional systems and procedures.

97. The Program is built around two design elements that draw on international best practice, but are tailored to the policy reform environment in Tunisia: (i) the variable but generally well-demonstrated absorptive capacity of the LGs for implementing investments, the proven management and administrative capacity of the CPSCL, the soundness of the primary planning vehicle (the PIC), and the robustness of the key operating systems such as procurement practices, justify the inclusion of all 264 LGs under the Program. In addition, the size of the resource transfers will remain consistent with past allocation levels. Consequently, the delta will not be in managing major grant increases, but in incentivizing and supporting the LGs, through the introduction of a performance based system, to adjust to the reforms that will focus on strengthening their governance and sustainability functions and financial management capabilities; and (ii) the size and/or the advantageous characteristics of the unconditional capital grant have to be sufficient to incentivize LGs to seek access to it, and therefore to be motivated to improve their performance – the scale of the unconditional grant, while not significantly larger than previous funding levels, is the primary source of investment funds for the LGs, and it will be available entirely for their discretionary use for infrastructure investment purposes.

98. The reforms introduced under the Program are all incorporated into the revised Decree and directly address key features of the existing system that currently either embed the *"tutelle"* system, or over time have had increasingly perverse effects as follows:

- *The system for allocating grants has not been transparent*. Under the Program, a formula has been introduced that is based on considerations of distributive equity (population has been used for this – 80 percent), and redistributive considerations as measured by fiscal capacity (a proxy for the strength of the economic base - 20 percent).

- *Grant access requirements under the previous version of the Decree that linked the use of grant funds to requirement to utilize loan funds in predetermined ratios have led to serious levels of fiscal stress* in nearly half the LGs. Under the reforms, these linkages have been terminated and the use of grant funds is subject only to council decisions on their investment priorities.

- *The prior linkage of grants to loans led to the well-endowed LGs being increasingly favored* as measured by the disproportionate per capita share of the grants they were able to garner, exacerbating regional disparities. The delinking, combined with the allocation formula addresses this issue directly, while still allowing the better-off LGs access to the loan funds to the maximum extent of their capacity to borrow.

- *The grant system undermined accountability of LGs to their citizens.* Under the reforms, the objective and predictable flow of funds, the unfettered responsibility of the LGs to determine the use of the funds, and the publication of LG performance data on the E-portal established under the Program, creates the space for consultation and accountability to be introduced and for social contracts to be built between LGs and their citizens.

- *There has been no system for assessing and monitoring LG performance.* Under the Program a system of performance requirements linked to grant access is being phased in with, ultimately, annual assessments being undertaken by an independent entity - the Controller-General of Public Services (CGSP).

99. The Program restructures the LG capital grant window to establish a channel for transferring conditional funds on a systematic basis to targeted Government priority initiatives. Currently, the Government runs a program that funds the provision of basic infrastructure service in disadvantaged neighborhoods on a relatively ad hoc basis, and that is operated relatively independently of LGs. The Program assists the Government in better aligning the upgrading program with its decentralization policy agenda and systematizing the process. The immediate impact of this change under the Program is that the process of consultation with affected communities is enhanced and the level of ex-post scrutiny in introduced by ensuring that key elements of the performance system are applied to the use of funds under this window.

100. The strategy under the Program of using the linkage of LG access to grant funds to leverage improvements in their institutional performance is underpinned by providing targeted capacity enhancement measures**.** Linking the access to funds with performance serves as a powerful means of leveraging LG utilization of capacity support systems. The Program provides the CPSCL, through their regional offices, with resources to contract skills on a just-in-time basis to respond to on-the-job capacity support to LGs. This approach has been selected because: (i) international experience has shown that approaches which offer this type of demand-responsive assistance to address real-time needs, and do so within the context of the day-to-day operations of the LGs, have proven particularly effective; and (ii) the CPSCL's six regional offices have proven capacity and well established working relationships with the LGs within their regions.

Expenditure Framework

101. The Program's expenditure framework relies on existing systems, and is expected to improve the funding predictability and financial sustainability of municipal capital investment.

102. The country has long operated on the basis of fiscal arrangements whereby grant funds are transferred annually to LGs through several windows, one of which is for capital investment purposes. The proposed Program is therefore grounded within this national fiscal architecture and operating experience and its primary contribution in addressing the decentralization provisions of the new Constitution is the reform of the capital grant system and the linkages of the reforms to strengthening LG performance. Under the revised capital grant system, the full annual allocation to which the LG is entitled will be released in a single annual disbursement at the beginning of the CY into the account of each respective LG within the Treasury, and will be available for use by the LG according to existing fund flow mechanisms and practices. The use of funds will be limited to those eligible local capital development services that fall within the mandate of LGs. The Program will use the well-established disbursement channels which form part of the Tunisian budget system, with the one change that the funds will only flow through the CPSCL for administrative purposes, but will not be held by them to disburse; rather, the funds will be held by Treasury to the account of each LG and will be released against expenditures as per existing processes.

103. Second, the resource allocations under the Program are of similar orders of magnitude in real terms to those that have been managed through the capital grant window over several five-year investment plan cycles. Table 7 summarizes the various components of the PIC as projected and then actually utilized over the past 10 years and compares them to the proposals by the Government for the Program cycle. While the estimates for the OSRs and the loans may be on the high side, the proposed capital grant component for 2014 to 2019 of TDN 305 million is equivalent to approximately US$200 million, or about US$5.7 per capita per annum. This represents a slight increase in real terms but remains at levels similar to those funded by the Government over the past 20 years. More particularly, as a share of the national budget, these levels have fallen. Expenditure patterns by the LGs demonstrate that they have been able to fully absorb and utilize the grants. Consequently, the project is designed to maintain affordable levels of investment similar to those that have been sustained in the annual budget over many years. This level of investment is designed to ensure that resource flows for local services do not fall, while using the period of Program implementation to establish a platform of regulations, systems and practices that can then be scaled up as appropriate and affordable to meet national investment priorities within the framework of the budget and the Constitution.

Table 7: Comparison of PIC allocations over three PIC cycles (2002 to 2019)

Funding Source	**PIC 2002-2006 TDN Million**		**PIC 2007-2011 TDN Million**		**PIC 2014-2019 TDN Million**
	Projected	**Utilized**	**Projected**	**Utilized**	**Projected**
OSRs	170.8	124.2	179.1	121.0	193.0
Loans	302.4	257.5	306.0	260.5	389.0
Grants	209.2	214.6	261.1	267.0	305.0
Total	682.4	596.3	746.2	648.5	887.0

104. Third, the Program complements the system of incentives for strengthening LG institutional capabilities that underlie the revised capital grant system, with a system of capacity support measures that international experience has demonstrated to be effective and an important factor in establishing capable LGs.

105. Finally, the sustainability of the reforms is underpinned by a system of capacity support to the central agencies tasked with oversight and support responsibilities, in order to assist them in making the transition from their traditional roles under the *"tutelle"* system to one of facilitation based on monitoring and evaluation, policy adjustment in response to issues identified through the Monitoring and Evaluation (M&E) system, and targeted support as needed.

Results Framework and Monitoring and Evaluation Capacity

106. The Program's results framework is designed to track the progress under three key areas: (i) improved inter-governmental fiscal transfer framework to provide transparent and predictable capital grants to all municipalities in Tunisia; (ii) improved capacity and performance at the municipal level; and (iii) improved access to municipal infrastructure in poor urban areas.

107. The CPSCL will have the responsibility of collecting the information and reporting on the indicators identified as part of the Program's results framework. The primary sources of information will be the Annual Performance Assessment to be prepared by the Controller General of Public Services *(Contrôleur Général des Services Publics,CGSP)*, and the technical progress reports submitted by the LGs to the CPSCL.

108. The capacity required from the CPSCL to manage the Program's M&E requirement is commensurate with the CPSCL's earlier role in terms of prior review of the LGs' individual investment proposal. In addition to CPSCL's existing system, the Program will support the development of an IT platform hosted and managed by DGCPL to disclose information and key documents related to LGs' performance (E-Portal), both on service delivery and participatory governance initiatives.

Economic analysis

109. The following economic analysis contains several analyses. It provides an analysis of the development impact of the Program through economic return, alternative project, risk, and fiscal sustainability analyses of this project. It outlines measures to facilitate continued economic analysis of the project, provides a rationale for public sector provision and financing, and explains World Bank value-added.

Development Impact

110. The expected development impacts of the Program are improvements in: the infrastructure and services provided by local Governments (LGs) in Tunisia for all of their residents; LG capability to deliver infrastructure and services; and the relationship between Tunisians and their Government. Despite gains in access to infrastructure and basic services in Tunisia over the past two decades, large disparities remain in access to basic services administered by LGs (namely public sanitation networks and local roads). Approximately 25 percent of Tunisians are disconnected from a public sanitation network with substantial differences in access within and across LGs.[10] Poor sanitation network connections can lead to higher incidences of illnesses such as diarrhea compromising the health of relevant populations and their financial resources due to the costs associated with these illnesses. In 2004, a study estimated that the annual costs associated with diarrheal incidence in Tunisia were between 11 and 56 million TND.[11] Citizen discontent with services under the mandate of LGs was

[10] For instance, only 7% of homes in Tunis have no connection to the public sewerage system while 88% of homes in Sidi Bouzid do not have access to public sanitation service (WB 2013).

indicated in a recent survey conducted by the Bank on Tunisian citizen perceptions of Government provision of services. Poor local road networks are associated with constrained access to markets. The January 2011 Revolution highlighted the grievances of marginalized populations in Tunisia and the large-scale impact neglecting those grievances can have on development and prosperity across the country; as such, the dual goals of helping marginalized Tunisians attain a minimum standard of quality of life and improving the relationship between citizens and Government are urgent priorities for the Government. More detailed economic analyses of the project are provided below.

Economic Rate of Return

111. The measurement of economic rates of return (ERRs) for LG strengthening programs is not straightforward for several reasons. Reform of the inter-governmental capital grant system is designed to empower LGs and their citizens, hence the specific investment projects that will be financed through the grant(s) supported through this Program are unknown at this stage. Furthermore, the projects that can be undertaken by LGs with the support of this Program – particularly local roads, drainage network connections, and street lighting – are small-scale with many of the benefits non-rigorously quantifiable. The Government has not mandated economic analyses for these types of projects in the past, hence no data exists that could be used to quantify the benefits of similar projects in Tunisia. Rate of return analysis is even more difficult to do in a rigorous and credible manner for institutional development strengthening activities.

112. Nevertheless, there is evidence of positive returns for some similar Local Government support projects that have been supported by the World Bank in other countries. In Uganda, an assessment of the first Local Government Development Program (LGDP1) found that the ERR of the small infrastructure projects provided through LGs was above 12 percent.[12] A similar project in the Philippines – the Local Government Finance and Development Project – yielded an ERR of 35 percent.[13] Although the context and the exact bundle of investment projects vary, these findings indicate that if well-designed and implemented, this Program could generate positive economic returns. It is proposed that feasibility studies for any investments estimated to cost more than US$1.0 million undertaken by the LGs under the Program will require ERRs to be included and this will be captured as part of the annual PAs. It is also proposed that a program for undertaking social and economic impact analyses of selected LGs, designed to provide indicative data on qualitative outcomes, would be undertaken during the course of Program implementation.

Productive Efficiency

113. The proposed reform of the inter-governmental capital grant transfer system and the institutional development strengthening activities are expected to increase the productive efficiency of LGs. Productive efficiency has been achieved in settings where citizens were better able to hold LGs to account, where fewer tiers of Government were involved in service delivery and the tier providing the services had better knowledge of local costs.[14] World Bank studies have found that in many cases, infrastructure delivered in decentralized contexts was of higher quality and was completed at lower cost than in more centralized settings, and that results-based approaches to municipal development achieved more sustained impacts.[15] For instance, the cost effectiveness of local roads produced in the Uganda LGDP-I project was in the range of 32.6 - 38.9 percent of the total investment.[16] Furthermore, the greater

[12] World Bank ICR 2008
[13] World Bank ICR 2009
[14] Kahkonen and Lanyi 2001
[15] Martinez-Vasquez 2011, IEG 2008, and UNCDF 2008.
[16] World Bank ICR 2008

scope for decision-making, technical support to enhance learning by doing, and accountability loops introduced through this project are expected to help increase the organizational performance of LGs.

Allocative efficiency

114. Greater discretion[17] over the use of their resources is expected to improve the allocative efficiency of LG infrastructure and service provision. International experience demonstrates that LGs are capable of better allocating resources according to citizen preferences than central Governments when they have adequate discretion over the use of resources and when citizens can monitor local Government performance.[18]

Alternative Project Considerations

115. Several alternatives could have been pursued in place of the proposed Program. One option would have been for the Government to continue with business as usual. Under this scenario, the deterioration of the provision of LG services and infrastructure, and the financial health of LGs was likely to continue. Alternatively, the Government could have pursued an emergency project to provide basic infrastructure and services through central authorities rather than through LGs. This measure could have been justified on the grounds of the urgent need to address these basic needs of citizens and alleviate social tensions associated with the 2011 Revolution. However, it would have further undermined LG authority. It also would have foregone a critical opportunity to foster accountability mechanisms between citizens and the Government. Other program design parameters could have been altered, and several such considerations were made during Program preparation, but the proposed design reflects a consensus regarding the design that promoted the greatest development impact given existing constraints.

Rationale for Public Sector Provision and Financing

There is a strong rationale for public financing of the activities supported under the Program. Specifically, the rationale for public sector provision and financing is that: (i) the investments are local public goods; and (ii) no negative substitution effects are anticipated.

116. *Most of the Program investments are in public goods.* The municipal investments eligible for support under the unconditional and conditional grants are mostly local public goods, and therefore likely to be undersupplied by the market. These include municipal roads, street lighting, drainage, water supply and sanitation, solid waste management, and local social and economic infrastructure. The provision of these goods is under the responsibility of LGs as per the 2014 Constitution, in keeping with commitment to achieve a more efficient and closer administration to citizens.

117. *No negative substitution effects.* The Program focuses on improving the efficiency of transfers for infrastructure investment and capacity of LGs to select and implement projects. It is therefore not expected to lead to any substitution effects on infrastructure investment. The projects will continue to be selected through guidelines for preparation and evaluation of subprojects outlined in the Program operations manual, [19] although LGs will be given full responsibility and autonomy for the selection, preparation and execution of local investments supported by the grants. The allocation and

[17] Combined with greater citizen participation and enhanced accountability mechanisms.
[18] For example, local budgets better matched citizen priorities after further decentralization in Uganda & the Philippines (Martinez-Vasquez 2011).

implementation of funds is therefore expected to improve with the project, and is not expected to have any new negative substitution effects.

World Bank Value-Added

118. The World Bank adds value to the Program through financing, relevant and operational expertise, and by its ability to help leverage additional resources.

119. The institution has extensive experience supporting inter-governmental fiscal transfer system reforms, programs to strengthen LG capabilities, and programs to increase access to municipal services and infrastructure in Tunisia and around the world. The World Bank has supported consecutive municipal development programs in Tunisia since 1992. More broadly, the World Bank has supported decentralization efforts in more than 89 countries in the world since the 1990s, including in Morocco, Jordan and West Bank and Gaza in the Middle East.[20] An IEG assessment of a subset of World Bank decentralization operations found that the impact of many of these operations was weak in the 1990s but improved considerably in the 2000s.[21] This improvement may be attributable in part to World Bank staff disseminating lessons learned as appropriate to other projects over time. These lessons range from the importance of pairing certain reforms to the necessity of having effective performance monitoring systems in place and in use. Such lessons have been reviewed and have informed the World Bank's engagement with Tunisia on this Program.

120. Furthermore, the World Bank can help relevant parties in the Government leverage support for its LG development program as it undertakes this set of reforms in a politically challenging environment. Reform of the distribution of national wealth, and of formal linkages and practices that change the relationship between different levels of Government and between Government and society are by definition challenging to accomplish. The current socio-political context provides both an impetus and a constraint to the successful introduction and implementation of such reforms. The involvement of a relatively neutral actor – the World Bank – in helping facilitate the national dialogue and deliberations needed to define and introduce these reforms can help accelerate and improve the outcomes of these efforts. Furthermore, the Bank's commitment to this reform program has helped attract additional development partners to support certain dimensions of the reform program.

B. Fiduciary

121. As part of the preparation of the Program, the Bank task team carried out a Fiduciary Systems Assessment (FSA) of the Program in accordance with OP/BP 9.0. Based on the findings of the FSA, it is concluded that Program Fiduciary Systems have the capabilities to provide reasonable assurance that the financing proceeds will be used for intended purposes. However, considering the existing weaknesses in Program Fiduciary systems, the residual fiduciary risk rating for the Program is rated as Substantial.

122. The Program will finance a portion of the grant components of the Government's existing program for financing municipal service delivery that involves a combination of capital grants and loans in addition to the own source revenues generated by the LGs themselves. The Program intends to reform the system of capital grants by making it predictable and based on an allocation formula that is principle based and transparent. Indicative allocations for capital grants will be included in the five-year and annual investment plans and indicative allocations will be communicated by MoEF through the CPSCL in advance of the annual plan preparations. The budget allocations for capital grants will be transferred from the Treasury Current Account at the Central Bank of Tunisia (BCT) to CPSCL as part of existing

[20] IEG 2007
[21] IEG 2008

state budget implementation procedures. CPSCL will in turn transfer the grant funds to LGs in accordance with the operating rules for the Capital Block Grants and Conditional grants as determined by the Decree. During the first two years of the Program (Calendar years 2014 and 2015), given the transition LGs are going through, the share of Capital Block Grants allocated by LGs to finance investments co-financed by a loan from CPSCL will be transferred to the respective LG's designated account at the CPSCL. The remaining amounts will be directly transferred to the LG's treasury account.

123. Assessment of the Program expenditure framework shows that in addition to the changes in the design of the capital grants through the proposed decree, additional steps such as communicating the indicative allocations of capital grants in advance and reforming the existing system of multiple ex-ante checks and controls into a coordinated system of ex-post controls such as annual audits are necessary for the efficient implementation of the proposed Program.

124. Municipalities will utilize capital grants to implement various investment projects that are approved under their five-year and annual plans and are included in their annual budget. All municipalities are staffed with the technical, financial management and procurement skills required for management of the municipal work program. Municipalities have financial managements systems adequate for the custody, accounting and reporting of Program funds. The expenditure cycle for municipalities is submitted to the same controls applicable for the Central Government. The General Expenditure Control Unit *(Contrôle Général des Dépenses)* under the Prime Minister's office has to approve ex-ante, at the commitment stage, every single expense through the ADEB system. Then the municipal accountant (*receveur*) has to control the whole process and the justifications before making the payment (*contrôle concomitant*). Municipalities are subject to the oversight and supervision of the General Inspectorate of the Ministry of Interior, by the *Contrôle Général des Finances* (Internal Audit of the MoEF) and the Court of Auditors *(Cour des Comptes)*.

125. The controls and audit framework related to LGs provides some level of fiduciary comfort but at the same time constitutes a major risk of not achieving desired results due to their weaknesses in implementation and capacity. The Program design has included a set of Mandatory Minimum Conditions (MMCs) that municipalities need to comply with before getting access to the capital grant funds. Most of the MMCs relate to actions that municipalities are required to comply with according to the existing legal and regulatory framework and thereby provide a degree of fiduciary assurance. For strengthening the accountability framework of municipalities it has been agreed with the Court of Auditors *(Cour des Comptes)* that they will carry out annual financial audit of municipalities. The annual financial audit of municipalities will be implemented in a phased manner with the objective of bringing the majority of municipalities under the scope of the annual audit by the end of the Program. The capacity-building element of the Program will provide the necessary support to the Court of Auditors *(Cour des Comptes)* to carry out the annual audits in time.

126. Procurement processes and systems at the municipal level are adequate for the efficient implementation of the Program. Despite the weak capacity of smaller municipalities, procurement processes in LGs are found to be more efficient than even many line Ministries' at the central level, in terms of the time required to complete the procurement process. The assessment of a sample of municipalities/LGs has shown that the overall duration of the procurement process is shorter in LGs when compared to central bodies and Ministries. Also since the municipalities have an annual investment program and are more under direct pressure of local population to actually provide the infrastructures or services needed, there is a sense of urgency to expedite the procurement process despite the excessive number of prior controls and clearances. Tunisia has recently promulgated a new decree for public procurement that emphasizes transparency and efficiency and the provisions of which will apply to LGs as well. LG compliance with national procurement regulations is also found to be good. Tunisia has a functioning institutional structure for the handling of complaints relating to public

procurement. The Public Procurement Oversight Committee *(Haute Instance de la Commande Publique, HICOP)* provides overall technical guidance on public procurement and monitors the compliance of procurement standards and practices. The Procurement Monitoring Committee (COSEM) receives complaints relating to public procurement and takes follow-up action. As part of the Program design, and in order to address the risk of delays to the procurement process caused by the multiple and overlapping controls, it has been agreed that the municipalities will not be required to obtain the prior clearance/approval from the CPCSL for investments made under the Program. This is expected to reduce the average duration of the municipal procurement process under the Program. The Program Action Plan also recommends that a procurement capacity- building program be designed, after a systematic assessment of LG requirements has been undertaken, and that it be implemented as part of the capacity-building element of the Program. To enhance the transparency of the procurement process, all contracts awarded by municipalities will be displayed in the national procurement portal of the "observatory".

127. The design of the Program relies on many of the existing institutions and processes for addressing fraud and corruption risks of the Program. The Program will interface with existing institutions of Governance like HICOP, COSEM, as well as the State Secretariat for Public Governance (*Secrétariat d'Etat à la Gouvernance et à la Fonction Publique)*. Tunisia has recently formulated a National Strategy on Anticorruption that is based on the International Convention on Anticorruption. There is a high powered body in the Prime Minister's office that will be responsible for the implementation of the strategy and all Government programs (including the Program) will be under the scope of the body. The National Authority for Fighting Corruption (*Instance Nationale de Lutte contre la Corruption*) is responsible for investigation of complaints relating to corruption. In addition, there is an Anticorruption hot line and a website where any citizen can file complaints/grievances which are both functional. Municipalities have a Citizens Relations Bureau where citizens can submit grievances. The CPSCL will maintain an up-to-date list of contractors debarred by the Bank and convey such information to all municipalities. The Program is financing the design and implementation of an E-Portal where all relevant information (both financial and operational) relating to the implementation of the projects that are part of the annual plan and budget will be displayed for public information. The municipalities will be preparing their plans and budgets in a participative manner in consultation with their citizens. The Performance Assessment of municipalities will include areas relating to transparency, accountability and participation in municipal management and the performance of each municipality on these areas will be evaluated.

128. As part of its responsibilities for coordinating Program implementation, the CPSCL will also be responsible for preparing the Program Financial Statements, compiling them from municipal financial reporting as well as financial reporting from other agencies, if any. The annual audit of the Program financial statements will be carried out by the Court of Auditors *(Cour des Comptes)*.

C. Environmental and Social Effects

129. An Environmental and Social System Assessment (ESSA) for the Program has been conducted by the World Bank in order to examine Tunisia's existing environmental and social management systems for municipal infrastructure projects and to ensure their consistency with the core principles outlined in OP/BP 9.00 Program-for-Results Financing. The draft final ESSA Reports in English and French were posted on the Bank's InfoShop on May 16, 2014, and were also made public by the World Bank Office in Tunis. The final ESSA reports were disclosed through the Bank's infoshop and in country on June 24th, 2014.

130. The ESSA analyzes the system for environmental and social management as it is and how the system is applied in practice in order to assess the constraints and gaps between those systems and the

Program's principles. Identified measures to fill those gaps and strengthen systems were incorporated in the overall Program design. The portfolio of projects to be undertaken was also analyzed to identify typical environmental and social effects (both positive and negative) for the types of projects that are eligible for financing under the Program. The ESSA was informed by a desk review of relevant laws, policies and regulations, and field visits to a representative sample of municipalities included in the Program, and a sound stakeholder consultation process. The draft ESSA was discussed in a consultation workshop with relevant stakeholders on April 16, 2014.

131. **Negative effects from Program activities are likely to have low to moderate environmental and social impacts.** Overall, the assessment concludes that the proposed activities and the applicable systems are in many ways consistent with the core principles of OP 9.00. However, there are some areas that need further strengthening. The Program activities that are likely to have environmental and social effects are those related to: (i) delivery of municipal infrastructure; and (ii) improving access to municipal infrastructure in disadvantaged neighborhoods. These activities include roads and paving, construction, rehabilitation and upgrading, street lighting, sewerage extension/connection to public network, storm water drainage, solid waste collection, parks and some recreation facilities, markets, small-scale rehabilitation of slaughterhouses, and other environmental improvements.

132. Based on the type, scope and scale of works allowable under this program, adverse effects are expected to be typical construction impacts that are site-specific and generally limited to the construction phase. Similarly, given the scope of activities, it is highly unlikely that resettlement would occur, although land acquisition may be required for the construction of infrastructure works, for example in widening roads in the existing rights-of-way or acquiring land for new market areas. This has the potential to impact land, assets, property, crops, and shared community facilities such as water points, community roads, and roadside markets. Because of the significant geographic dispersion of the participating municipalities and the scale of proposed investments, cumulative effects of the Program as a whole are unlikely. As described below and in more detail in Annex 6, a screening process for all projects includes criteria to exclude certain types of projects (e.g., new landfills and wastewater treatment plants) as well as projects of a scale that would include significant negative impacts that are sensitive, diverse, or unprecedented on the environment and/or affected people (such as new slaughterhouses which are excluded from financing and ineligible under the Program).

133. **The system for environmental and social management of the Program will be largely based on the existing legal, regulatory and institutional system for environmental and social assessment and management in Tunisia**. The Program will draw on experience on similar programs over the past 20 years in Tunisia. The Government agency responsible for supporting the funding of municipal investment plans (CPSCL) has developed an Environmental Assessment Manual (2003) with Bank assistance for the management of such investment plans. The ESSA has found that the Tunisian system for environmental and social impact assessment is well established and relatively comprehensive, reflecting international practices. This system is in general sufficient to ensure that potential impacts will be identified and managed. However, some gaps and limitations must be addressed for compliance with the provision of the new constitution and the requirements of the OP 9.00. In addition, the system is constrained by human resource gaps at various levels, and its implementation is at times inadequate as personnel frequently lack the required qualifications (e.g., to make site inspection visits, or to adequately carry out consultations).

134. In fact, Tunisia has a relatively advanced environmental assessment framework that was introduced in 1991 and updated in 2005. This framework is now well established, integrated into the process of decision-making, and ensures proper handling of the environmental impacts of new projects subject to Environmental Impact Assessment (EIA). The framework is differentiated by a potential impact: a detailed EIA to be submitted to the National Environmental Protection Agency (ANPE) is

mandatory for projects with potential large-scale adverse impacts, a simple Environmental Assessment is required for projects with moderate adverse impacts; and Sectoral Environmental Standards (*Cahiers des charges sectoriels*) must be applied for projects with limited impacts. In this respect, the system allows for the detailed analysis of environmental impacts and identification of measures to be implemented to eliminate, mitigate or compensate adverse impacts to acceptable levels. An Environmental Management Plan (EMP) is routinely required for control and monitoring of compliance approved during the phases of construction and projects implementation. At the institutional level, the National Environmental Protection Agency (ANPE), a public institution responsible for the management of the EIA system has good experience and skills, particularly in the field of EIA review, monitoring of EMP implementation and environmental monitoring (air, water, and soil). On the expertise level, there are a number of firms and consultants who have adequate references and capacity in the field of environmental management. In addition, other stakeholders directly or indirectly involved in the system (authorities, petitioners, civil society, etc.) are familiar with the procedures used in the different stages of the EIA process and have benefited from several training sessions over the past 20 years. The EIA system has been able to gradually gain some legitimacy; however, it contains some gaps and limitations that must be addressed for compliance with the requirements of the OP 9.00. The main gaps are the lack of regulations and specific procedures to: (i) assess social impacts; (ii) consult public and affected populations and ensure their participation in decision-making processes; and (iii) disclosure of EIA documents.

135. Although Environmental Management Systems are present, capacity needs to be built at the municipal level, where weaknesses exist in environmental monitoring and supervision practices during the sub-project construction phase. Environmental considerations and mitigation measures are not adequately incorporated into technical proposals, contractor clauses and construction supervision clauses. Technical staff appointed at the city level often lack appropriate training and experience in environmental management. Environmental law enforcement is weak and the application of fines is limited. There is also a need to update the CPSCL's Environmental Manual which is over ten years old, particularly with regard to project categorization, public consultations and disclosure, and environmental supervision and monitoring. A first updated draft has been prepared and will be improved and disclosed by the CPSCL.

136. From a social perspective, gaps and weaknesses have been identified in involuntary resettlement, as well as in participation and social accountability practices. There is a need to upgrade the CPSCL's recently produced draft Resettlement Guidelines (*Plan cadre d'acquisition de terrains, 2013*) and to provide appropriate guidance to municipalities, particularly with regard to the resettlement and compensation of non-authorized commercial occupants of public lands and rights-of-way. Municipalities will need to ensure that people affected by loss of land and assets – in the unlikely event where this should occur in the context of municipal infrastructure sub-projects – are properly compensated and assisted in the restoration of their livelihoods. Attention needs to be paid to improving the transparency and accountability of implementing organizations. Guidelines need to be developed for effective participation and consultation with affected residents. Municipalities participating in the Program will also need to adopt effective grievance and redress mechanisms.

137. The overall risk from both environmental and social perspectives is rated as Moderate. To mitigate risks, the Program should help improve the national system for environmental and social impact assessment to fill identified gaps (assess social impacts, improve project categorization, and include public consultations and disclosure). From an environmental perspective, the environmental management capacity for the participating Government agencies and municipalities needs to be strengthened, and the environmental screening and assessment process and environmental monitoring and supervision needs to be improved. Community participation in sub-project design and construction monitoring should be promoted. These measures to improve the environmental and social management systems in line with the principles of OP 9.00 will be implemented through the Program Action Plan.

D. Integrated Risk Assessment Summary

Risk	**Rating**
Technical	Substantial
Fiduciary	Substantial
Environmental and Social	Moderate
Disbursement Linked Indicator	Moderate
Overall Risk	High

Risk Rating Explanation

138. While significant mitigation of identified risks is possible within the design of the Program, given the current political transition phase at both national and municipal levels and the novelty of the results-based approach and capacity issues at different levels, the overall risk is rated as High. The main risks can be summarized as follows.

139. **Political Uncertainties and Program Ownership.** While it is reassuring that Tunisia has already adopted its new Constitution with strong commitment from the state for the adoption and the implementation of the decentralization agenda, challenges and risks related to the political fluidity particularly at the local level (notably the uncertainty of the timing of local Government elections) may be faced during the operationalization of the proposed policy reforms. All of this creates uncertainty which may detract from investment and economic performance. It is difficult to mitigate the risk of political fluidity. The understanding of the international community together with financial and policy support from international financial institutions may help mitigate this risk.

140. While the Program's objective and expected outcomes are in line with many of the aspirations that led to the Revolution, it will be important to ensure their ownership by the Government. Also, some reforms supported under the Program such as the capital grant reforms have proved to be difficult to implement and present a risk of capture by groups within the line ministries and the MoEF. To mitigate risk, challenging activities and proposed reforms have been lengthily discussed with the counterparts during preparation and the Program builds upon a suite of ongoing and solid dialogue on decentralization and local governance reform with the support of the ongoing Bank funded Tunisia Urban TA program. In addition, appropriate consultations and assistance to stakeholders have been carried out at all relevant stages of Program preparation. Also, the Program is in line with the key priorities outlined by the Government program to support local authorities as outlined in their letter to the Bank dated January 2, 2014. Finally, the demand-driven approach retained for most of the Program activities offers flexibility to take into consideration feedback from new municipal councils as soon as they are on board.

141. **Technical.** Although the CPSCL in charge of coordination of day-to-day implementation of the Program has significant experience implementing similar municipal investment programs with World Bank support, capacity to appraise, monitor and supervise infrastructure projects is modest particularly in small cities. Sustainability of infrastructure investments will be weak if technical designs are not

optimized. This risk will be managed through good technical assistance including intensive training and continuous support during Program implementation.

142. **Fiduciary**. The main risks relate to multiple ex-ante controls exercised by the Central Government as part of the existing "*tutelle*", weak municipal systems for budgeting, accounting and financial reporting, gaps in existing procurement practices, inability of audit agencies to carry out external audits of municipalities on an annual basis, weak municipal staff capacities in financial management and procurement, and capacity and weak governance and anti-corruption systems. Though the Government has put in place a national strategy on anti-corruption, implementation arrangements are lagging. Therefore fiduciary risk is considered initially to be high. However, several mitigation measures are currently being designed which will result in the residual risk rating to be substantial.

143. **Environment and Social.** The ESSA has found that the Tunisian system for environmental and social impact assessment is well established and relatively comprehensive, reflecting international practices. This system is in general sufficient to ensure that potential impacts will be identified and managed. However, some gaps and limitations must be addressed for compliance with the provision of the new constitution and the requirements of the OP 9.00. In addition, the system is constrained by human resource gaps at various levels, and its implementation is at times inadequate as personnel frequently lack the required qualifications (e.g., to make site inspection visits, or to adequately carry out consultations). From a social perspective, gaps and weaknesses have been identified in involuntary resettlement, as well as in participation and social accountability practices. The environmental and social risk rating of the program is deemed to be moderate, and can be mitigated through technical assistance. Measures to mitigate identified environmental and social gaps in the Tunisian system are provided in the Program Action Plan.

E. Program Action Plan

144. While built on a sound legal and regulatory foundation as well as on the experience and momentum gained during the previous five-year municipal investment plans and the related Bank support, the Program will benefit from additional actions to facilitate effective implementation and meet international good practice. The Program Action Plan contains the key actions that will be taken in the course of Program implementation. These actions are included in Annex 8 and summarized in the Table 5 below.

Table 8: Program Action Plan

Area 1 – Transparent capital grant system
1. Decree 97-1135 replaced to introduce transparent formula based allocation of capital grant for municipal infrastructure delivery
2. Ministerial Decree issued indicating the annual allocation formula and MMCs applicable to capital grant for municipal infrastructure delivery
Area 2 – Municipal performance assessment
3. Preparation and approval of the LG Performance Assessment Manual
4. E-portal designed and operational
Area 3 – Municipal capacity-building
5. Annual Capacity Development Plans prepared by all LGs
6. Preparation of standard terms of reference for feasibility studies of investments in disadvantaged neighborhoods
7. Environmental and Social Manual (ESM) developed that provides updated procedures for environmental and social management for LGs to address gaps identified in the ESSA, including: (i) public consultations, public disclosure and grievance redress mechanisms; (ii) social assessment; (iii) land acquisition and resettlement procedures; (iv) screening of high-risk activities which are ineligible for Program support; and (v) monitoring and evaluation.
8. Specific training modules consistent with the provisions of the POM have been developed and are made available to the LGs.
9. Specific training modules on financial management for municipal financial management staff are developed and a national wide training program is initiated.
Area 4 - Country systems improvement
10. A revised decree is adopted by the ANPE which addresses gaps identified in the ESSA, including (i) screening and categorization of activities requiring an EIA or an EMP; (ii) public consultations, public disclosure and grievance mechanisms; (iii) social assessment; and (iv) monitoring and evaluation.
11. The capacity of the *Cour des comptes* and in particular its local branches is improved in order to perform annual financial audits of municipalities based on risk and in compliance with international norms of auditing (ISSAI).
12. Municipalities to prepare and implement annual action plans to address audit findings within a period of six months after the receipt of the audit report.
13. Citizen’s Bureau in each municipality to be operationalized and their performance in grievance resolution monitored by the municipal councils.
14. Good Governance Cells established in all municipalities by the second year of the Program.

V. ANNEXES

Annex 1: Detailed Program Description

I. The Government Program

1. Recognizing that decentralization is a longer term process, the Government has proposed a phased approach to LG reform, taking into account the importance of showing results on the ground now. The Government is therefore introducing a near-term program comprising key elements that: (i) can be immediately and practically introduced; (ii) lay the groundwork and have the maximum impact possible for introducing key reforms embedded in the decentralization objectives of the Constitution; (iii) focus on strengthening the capability of LGs to be better able to deliver local municipal services, and to do so in a manner that is fully accountable to their citizens; (iv) address disparities between LGs and regions in local service levels; and (v) at a minimum sustain planned levels of investment in local municipal services while creating the platform for future scaling up.

2. Specifically, the Government has recognized that the restructuring of the capital grant system for transferring investment resources to LGs, governed by the Decree 97-1135, can be undertaken early on and offers significant opportunities to establish greater accountability between LGs and their citizens, as well as concurrently building the institutional capacity of the LGs to better deliver local services. The revision of the Decree is pivotal to the operation of LG capital grant system, and lies at the heart of the reforms necessary to address the issues identified above and respond to the decentralization mandate of the constitution. The changes to the decree that are necessary to underpin the first phase of the Government's decentralization reforms include:

- Separating the access of LGs to capital grants from the requirement to borrow and to mobilize own source revenues, thus removing one of the key drivers of growing municipal fiscal stress, as well as leveling the playing field so that the fiscally stronger LGs don't gain disproportionate shares of the grant;
- Ensuring transparency in the capital grant allocation system and enhancing accountability between local LGs and their citizens by introducing formula-based annual transfers that are constructed around objective, measurable criteria, and that ensure predictability of fund flows in order to enhance efficient planning by the LGs;
- Providing timely indicative annual allocations to the LGs to facilitate their ability to undertake participative municipal investment planning and efficient use of resources;
- Progressively introducing an independent, annual performance assessment system to strengthen LGs' institutional capacities for better service delivery and to facilitate greater citizen access to information;
- Publishing of the findings of the performance assessment in a timely manner; and
- Removing ex ante central controls over capital grant planning and utilization, thus enabling use of capital grants to be determined at the discretion of LGs.

3. In this context, the Government program consists of delivering municipal infrastructure services in an accountable and responsive manner through a mix of grants, own source revenues and loans, as well as institutional strengthening of the 264 municipalities for the period 2014-2019. Through this program, the Government intends to shift from a purely "infrastructure delivery" approach to a greater focus on LG performance and accountability**.** To this end, the Government's program aims at: (i) strengthening LG institutional capabilities; (ii) transforming their relationship with their citizens through measures that are designed to foster transparency, participation and accountability; and (iii) improving the municipal infrastructure delivery with special attention to disadvantaged communities.

4. The Government program consists of three sub-programs, namely:

- Subprogram 1: Municipal infrastructure delivery;
- Subprogram 2: Improving access to municipal infrastructure in disadvantaged neighborhoods;
- Subprogram 3: Capacity support for improved LG institutional development and accountability.

Subprogram 1: Municipal infrastructure delivery (US$591 million)

5. Consistent with past practice under the PIC, the subprogram involves the preparation of five-year investment plans for each LG to deliver municipal infrastructure. Activities under the subprogram will include consultancy services (including feasibility and engineering studies, and support to implementation services) and civil works directly linked to LGs core mandates such as roads and paving, construction, rehabilitation and upgrading, street lighting, sewerage extension/connection to public network, storm water drainage, solid waste collection, parks and some recreation facilities, markets, and other environmental improvements.

6. The financing framework for the activities under this subprogram includes three sources of finance: (i) LG contribution; (ii) capital grants from central Government; and (iii) investment loans provided by the CPSCL. These sources of finance are discussed in the following paragraphs.

7. **Capital Block Grants for Municipal Infrastructure Delivery (US$203 million).** The use of capital grants for municipal infrastructure delivery is determined solely at the discretion of each LG (without any ex ante control), subject to being used for municipal infrastructure investments that fall within the mandates of the LGs. It will be allocated on the basis of a formula and the use of these resources is determined solely at the discretion of each LG (without any ex ante controls), reflected in their annual investment plan and subject to their being used for municipal infrastructure investments that fall within the mandates of the LGs. LGs will receive unconditional capital grants from the CPSCL (on behalf of the state) to support priority investments in urban infrastructure that have been validated through a participatory planning approach and reflected in the LG municipal investment five-year and annual plans (PIC). The LGs will be responsible for planning and implementing sub-projects financed with the unconditional capital grant funds, grant funds will be reflected in the revenues and expenditures of the LG annual budgets and assets incorporated into their asset registers. Sub-project implementation will be undertaken by LGs with the support, if needed, of deconcentrated public agencies and private entities.

8. The unconditional capital grants will function according to the following principles:

a) a PIC whereby each LG is allocated an indicative envelope of resources available to it for capital investments over a five year period, to be transferred annually at the beginning of each CY;
b) the allocation formula is to be made public, as are the annual allocations to each LG;
c) the allocation formula is built around objective, measurable criteria that also include equalization considerations;
d) use of the funds is discretionary to the receiving LG and is not subject to ex ante review by central agencies;
e) access to the funds, which can be integrated with other untied LG revenues at the local level, is not tied to other parallel fiscal or financial instruments;
f) LG performance is assessed annually, ex post, by an independent evaluator, whose findings are made public and are presented comparatively across all LGs; and
g) performance assessment criteria cover three areas:
   1) Governance, comprising consideration of:
      (i) participatory planning and budgeting;

(ii) transparency in LG operations (access to information regarding: capital expenditures/consistency with budget, contract awards, investment implementation progress, financial statements/audits);
(iii) procurement (timeliness, efficiency and in accordance with regulations);
(iv) safeguards (planning and implementation procedures) and
(v) response to complaints;

2) **Sustainability**, including:
(i) asset inventory in place, asset management including O&M plans established annually and implemented;
(ii) where required, Financial Recovery Plans (FRPs) prepared and being implemented;
(iii) own source revenue collection enhancement plans prepared and being implemented; and
(iv) preparation and implementation of capacity building plans; and

3) **Management** addressing: investment implementation, financial accounting practices and satisfactory audits.

9. The total unconditional capital grants for municipal infrastructure amount to US$ 5.7 per capita/year. Key investment activities of the program include road construction, rehabilitation and upgrading, street lighting, urban drainage/sewerage and other environmental improvements, solid waste collection and street cleaning, parks and some recreation facilities, markets and slaughterhouses.

10. **Local Government Contribution (US$129 million).** In parallel with the above capital grants, the Government's 2014-2019 PIC envisages LGs contributions to increasing levels of investment in municipal infrastructure. The Government recognizes that reforming the own source revenue system will take time as it involves major policy changes, and is therefore focusing on opportunities for improving local revenue collection rates within existing tax and fee regimes.

11. **Municipal Investment Loans (US$259 million):** In addition, LGs capable to borrow will have access to the CPSCL credit line as a potential funding source to implement their Municipal Investment Plans (PIC). The Loans from the CPSCL serve to maximize leverage of resources available to LGs for investing in municipal infrastructure. In parallel, the Government is introducing reforms under the Decree and in the CPSCL lending guidelines in order to establish a stable balance between maximizing borrowings by the LGs and maintaining their financial viability.

Subprogram 2: Access to municipal infrastructure in disadvantaged neighborhoods (US$150 million)

12. Under this subprogram, the Government will provide targeted/conditional grants directed towards investments that represent national policy priorities (in this case, for the new PIC period, to improve access to municipal services in disadvantaged neighborhoods).

13. Due to resource constraints and the uneven distribution of disadvantaged neighborhoods across LGs in the country, a regional consultation process (involving elected officials from the National Constituent Assembly, representatives from regional and local Governments, civil society, and deconcentrated agencies) was undertaken to pre-identify neighborhoods and municipalities that would qualify to receive these grant funds during the CY2014-2019 cycle. Municipalities currently covered by ongoing urban upgrading programs are not targeted by the Program. As a result of these consultations 229 neighborhoods in 144 LGs have been identified.

14. Activities under the subprogram will include consultancy services (including feasibility and engineering studies, and support to implementation services) and civil works for the provision of basic infrastructure such as roads and paving, street lighting, sewerage extension/connection to public

network, and storm water drainage in selected disadvantaged neighborhoods located in 144 municipalities.

15. Tunisia has been implementing since 1992 national programs targeting upgrading of disadvantaged neighborhoods with the provision of basic municipal infrastructure (PNRQP). However, most of urban upgrading sub-projects were identified and prioritized by the center and implemented by the Agency for Urban Regeneration and Renovation (ARRU, *Agence de Rehabilitation et de Renovation Urbaine*), a dedicated national agency. LGs were merely consulted but had to co-finance up to 30 percent of the total cost.

16. The new approach will bring in innovations compared to past programs, particularly for: (i) full ownership and responsibility of LGs in preparing and implementing the related investments as part of their municipal investment programs; (ii) deep consultative and participatory approach for neighborhoods identification/prioritization and for neighborhood identification of priority investment needs; (iii) highly subsidized financing scheme aligned with the financial capacity of LGs to avoid existing additional municipal finance stress to access capital grants; and (iv) provision of just in time support to LG to implement sub-projects and develop capacity from the implementation.

17. The conditional grant allocation over the program period amounts to US$ 142 million or an average of about US$ 1 million per LG which represents around US$284/beneficiary (US$1420/household).

Subprogram 3: Capacity support for improved LG institutional development and accountability (US$10 million)

18. The Government's program upgrades the system of capacity support for LGs in order for them to achieve improved institutional performance targets. The capacity support program would contribute to the LGs ability to achieve the standards required under the performance assessment system to help them access their full entitlement to capital grants. Under this subprogram, LGs receive capacity development and technical support to prepare and implement their plans via training programs offered by CFAD and technical assistance from regional offices of the CPSCL and line agencies of central Government, as well as through local consultancy services.

19. An allocation of US$10 million will be committed through the national budget for the financing of this subprogram. Half of this amount is earmarked for technical assistance through framework contracts to be signed at the level of each regional office of the CPSCL for the provision of on demand technical assistance to LGs. This program being demand-based, the Government envisages the commitment of additional resources if assessed necessary during the Program's Mid-Term Review.

20. The Government program is summarized below in Table 1.1, with the grey shaded area of activities targeted by the PforR Program.

Table 1.1: Government's program and PforR Program scope

Subprogram 1 **Municipal infrastructure delivery** *TND 887 million (USD 591 million)*	**Subprogram 2** **Improving access to municipal infrastructure in disadvantaged neighborhoods** *TND 225 million (US$ 150 million)*	**Subprogram 3** **Capacity support for improved LG institutional development and accountability** *TND 15 million (US$ 10 million)*
Unconditional Capital Grants *TND 305 million (US$ 203 million)* Formula-based grant allocation to LGs subject to their meeting annual Minimum Mandatory Conditions (MMCs) and achieving satisfactory annual performance scores	**Conditional Capital Grants** *TND 225 million (US$150 million)* Grant allocation to LGs for specified investments in line with national priorities (currently for local infrastructure in disadvantaged neighborhoods), subject to their meeting a Minimum Mandatory Condition (MMC) grant access requirement	**Capacity building and technical support** *TND 15 million (US$ 10 million)* Demand-based capacity support to be provided to LGs on a just-in-time basis
LGs Contribution *TND 193 million (estimate)* LGs Contribution to the investments from their net savings		
Municipal investment loans *TND 389 million (estimate)* Investment loans to LGs from CPSCL		

II Program PforR: the Program

21. **Development Objective:** The objectives of the Program are: (i) to strengthen Local Governments' performance to deliver municipal infrastructure, and (ii) to improve access to services in targeted disadvantaged neighborhoods.

22. The Program will support most of the Government program activities with focus on capital grants for municipal infrastructure delivery and the institutional and capacity building elements:

23. **Duration:** Program implementation period is from 2014 to 2019.

24. **Geographic scope.** The Program will finance activities in the same geographical areas (the Program Area) covered by the Government: all 264 municipalities (LGs), plus any new ones that may be constituted during Program implementation.

25. **Sub-programs to be supported.** Based on the need identified during the preparation of the Government program and for increased selectivity of Bank support, the Program encompasses three primary activities: (a) capital block grants for municipal infrastructure delivery; (b) targeted capital grant for improving access to municipal infrastructure in disadvantaged neighborhoods; and (c) capacity support for improved LG institutional development.

A Capital Block Grants for Municipal Infrastructure

26. The capital block grants would be performance-based to incentivize LGs to achieve improved standards of institutional performance in key areas of their municipal functions. The target would be for 60 percent of LGs to achieve scores of 70 percent or more on their evaluation for the fifth year of the Program. To achieve the targeted outcomes, the Program provides resources under the unconditional grant sub-window for investments in local infrastructure services, with funding levels modulated by each LG's ability to meet annual performance standards applicable to unconditional grants as measured by annual Minimum Mandatory Conditions (MMCs) and Performance Assessments (PAs) undertaken according to agreed criteria.

27. Under the Program, 264 municipalities will receive capital block grants from the Government to support priority investments in urban infrastructure that have been identified and reflected in their participatory five year and annual municipal investment plans. The municipalities will be responsible for planning and implementing sub-projects financed with capital block grant funds, and grant funds will be reflected in the revenues and expenditures of their annual budgets.

28. Capital block grants will be allocated to the municipalities according to a transparent and predictable formula. These allocations are weighted by LG population and fiscal potential (80/20), subject to the application of an adjustment factor to ensure that each municipality will receive at least the equivalent of the envelope received during the previous PIC. These allocations provide an average annual allocation of US$ 29 per capita over the period of the Program, plus 12.5 percent compared to the current PIC.

29. These allocations are for planning purposes and the actual annual disbursement of funds will be made on the basis of verification of: (i) meeting the Minimum Mandatory Conditions (MMCs); and (ii) each city's performance measured against a set of criteria. The performance system consists of two levels of review, one comprising a set of Minimum Mandatory Conditions (MMCs), the other an annual Performance Assessment (PA) process.

Minimum Mandatory Conditions (MMCs)

30. The performance criteria to be met to satisfy the MMCs are derived from essential, minimum legal and regulatory provisions and also include core fiduciary requirements to assure satisfactory ex post oversight, as well as establish the basis for some of the performance standards to be included in the Performance Assessments (PAs). To this end the criteria comprising the MMCs will be incrementally introduced through the period leading up to the application of the PAs (2015 to 2017), as follows:

31. MMCs for accessing funds are as follows:

- The municipal budget for the forthcoming year has been adopted by the Municipal Council by December 31;
- The annual financial statement of the municipality for the previous year has been submitted to the *Cour des Comptes* for audit no later than May 31 of the current year;
- The annual municipal investment plan for the forthcoming year were produced according to satisfactory participatory procedures;
- The Municipality Procurement Plan for the forthcoming year has been uploaded onto the National Procurement website by December 31; and
- The Municipal Council has approved and the mayor has signed a Memorandum of Understanding with the Government through the CPSCL that will spell out the roles and responsibilities for both.

32. A municipality that is unable to satisfy all the MMCs is held to be ineligible to receive any grant resources for the forthcoming year. However, the funds remain assigned to the municipality's account and are reapportioned to it over the remaining years of the Program. In the event the municipality fails to qualify for two years running, the funds due it in the forthcoming year are returned to the pool of funds to be used for allocation to all the municipalities.

Annual Performance Assessment

33. An annual and independent Performance Assessment (PA) will be progressively introduced with effective implementation for the 264 municipalities during the third year of the Program. During the first two years, the Program will support the detailed design of the PA Manual, the preparation and organization of information and awareness events targeting municipalities and supporting agencies; and the implementation in 2016 of a dry run. The operation of the performance system will be refined and adjusted as necessary during the preparation of the PA manual and to take account of the experience gained through the dry run, but will remain consistent with the principles described above. Once fully operational (in 2017 to influence disbursements to LGs in 2018), the PAs will be implemented annually, and will be managed by an independent agency – the General Controller of Public Services (*Contrôleur Général des Services Publics*, cGSP).

34. Once the PAs have been phased in 2017 (for application to the 2018 grant allocation) both elements of the performance system (the MMCs and the PAs) will be applied. Thus, from year 2018 onwards, each LG, on satisfying the MMCs, will receive a disbursement of 40 percent of the funds available to them as determined by the allocation formula. Those municipalities scoring 70 percent or more on their PA scores will receive the remaining 60 percent of their allocation. For LGs unable to achieve the requisite score, the remaining share of their allocation for that year will be combined with the remaining funds they have been indicatively allocated under the five-year envelope and will be apportioned as per Table 4 for allocation in subsequent years. In the event an LG fails to meet the 70 percent score in two successive years, the funds for the forthcoming year will be reallocated for the remainder of the PIC period amongst all the municipalities.

35. During CY15 and CY16, the process will be repeated until CY17 when the PA system will be introduced. The PA exercise will start on May 1 of each year and be completed (including all reports required to present findings and recommendations) by August 31. Its findings would then be applied in time for the disbursements of grant funds in CY 2018 and all subsequent fiscal years. The differential phasing in of the MMCs and the PAs over four years, and the different weightings assigned between the MMCs and the PAs will have significant impacts in determining annual disbursement levels. Table 1.2 demonstrates the proportionate share of the annual disbursement that is determined by satisfying the MMC requirements and the proportionate share governed by the PA outcome, and sets out the disbursement profile based on 100 percent compliance of all LGs with the MMCs and the PAs.

Table 1.2: Annual Unconditional Grants Disbursement Mediated by the MMCs and the PAs

CY	**2015**		**2016**		**2017**		**2018**		**2019**	
US$ Total	22.1		33.15		44.2		60.775		60.775	
%/US$	**%**	**US$**	**%**	**US$**	**%**	**US$**	**%**	**US$**	**%**	**US$**
MMCs	100	22.1	100	33.15	100	44.2	40	24.31	40	24.31
PAs	0	0	0	0	0	0	60	36.465	60	36.465

36. **The PA component of the performance system will be detailed in a Performance Assessment Manual** that will be finalized and approved by June 30, 2015 and will be made fully operational in 2017

for determining disbursements for 2018. The objectives, contents and procedures of the PA manual will be introduced to the LGs through a series of regional workshops during the remainder of 2015. It will then be tested in 2016, in the form of a full-scale "dry run", and the results will be published to enable the LGs to determine their performance and, using capacity support offered under the Program, prepare an Action Plan to address areas where improvements are required. Concurrently, the process and content of the PA as operated under the dry run will be evaluated by an independent study commissioned by the CGSP and the PA manual will be adjusted to take account of the findings of the study.

37. **The PA will address of the following areas of LG competence**:

- **Governance**, comprising consideration of: (i) participatory planning and budgeting; (ii) transparency in LG operations (access to information regarding: capital expenditures/consistency with budget, contract awards, investment implementation progress, financial statements/audits); (iii) procurement (timeliness, efficiency and in accordance with regulations); (iv) safeguards (planning and implementation procedures) and (v) response to complaints;
- **Sustainability**, including: (i) asset inventory in place, asset management including O&M plans established annually and implemented; (ii) where required, Financial Recovery Plans (FRPs) prepared and being implemented; (iii) own source revenue collection enhancement plans prepared and being implemented; and (iv) preparation and implementation of capacity building plans; and
- **Management** addressing: investment implementation; financial management practices and satisfactory audits.

B. Conditional Capital Grants for Improving Access to Municipal Infrastructure in Disadvantaged Neighborhoods

38. Resources under the conditional grants sub-window for investments in local infrastructure services in targeted disadvantaged neighborhoods, with funding levels modulated by the participating LGs' ability to meet MMCs applicable to conditional grants that comprise the basic grant access element of the performance assessment system.

39. This conditional capital grants represent a vehicle for the Government to address policy priorities. Currently Government priority is focused on upgrading service levels in disadvantaged neighborhoods. A total of TDN225 million has been allocated under conditional grants for the PIC 2014-2019 period for this purpose. Due to resource constraints and the uneven distribution of disadvantaged neighborhoods across municipalities in the country, a regional consultation process (involving elected officials, city representatives, civil society, deconcentrated agencies) was undertaken to pre-identify neighborhoods and municipalities that would qualify to receive these grant funds during the CY2014-2019 cycle. Municipalities currently covered by ongoing urban upgrading programs are not targeted by the Program.

40. As a result of this regional consultation/selection process, 144 LGs comprising 229 neighborhoods have been pre-identified, and a preliminary estimate of the infrastructure requirements boundaries, number of households and costs has been established. To update these estimates and confirm their viability and scope, each participating LG will prepare a pre-feasibility study that will include participation of the affected communities, and will take into account the services to be improved, the size of the population and the level of poverty (requiring a brief survey), the levels and construction standards to be applied, the boundary of the selected neighborhoods, preliminary cost estimates, and the timeline for preparing and implementing the investments. Subject to the findings of the pre-feasibility studies, the LG councils will consider and, if approved, include the proposed investments within the framework of their annual plans and budgets.

41. The application of the performance system to the conditional grants is limited to the MMCs and then only on a one-time basis for the year when the construction of the approved upgrading plans is projected to commence. The same above MMCs for the unconditional apply the conditional grants**.** However, they are applied differentially. For the unconditional grants, it is an annual requirement and each LG has to meet the MMCs relevant for the forthcoming year in order to access any of the unconditional grant funds. Under the conditional grants, it is applied on a neighborhood-by-neighborhood basis for each targeted LG, and is a one-time requirement to access the conditional grants for that neighborhood. The MMCs relevant for the year in which the conditional grants are being sought are applied, but subject to the following additional provision: the completion of a pre-feasibility study (according to a format included in the Program Operations Manual) by each participating LG, and its approval by the LG council.

Box 3: Lessons Learned from previous LG development projects in Tunisia

C. Capacity support for improved LG institutional development and accountability

42. The Government's approach to capacity building in the LG sector is to address needs of the LGs, themselves, as well as key elements of the institutional framework, including operating systems, within which the LGs function. Higher levels of Government have a critical role to play in creating an enabling environment for municipalities, through providing sound regulatory frameworks, capacity support, and regular and effective appraisal and oversight.

43. The capacity support would contribute to the LGs ability to achieve the standards required under the performance assessment system in order for them to access their full entitlement to the capital grants. It will focus on the key support required to assist municipalities to achieve MMCs and performance criteria, and thus contribute to the achievement of the Program Development Objective.

44. Given the heterogeneous demand from municipalities, capacity and technical support will be provided based on an annual LG Capacity Development Plan (LGCDP) that will be prepared by each LG to address its needs. A preliminary capacity needs assessment was carried out during Program preparation and four broad areas were identified as requiring capacity building support at the city level including: (i) municipal investment prioritization and planning, including citizen participation and oversight; (ii) financial management including own source revenue enhancement; (iii) project quality, including procurement and environmental and social management; and (iv) asset management systems and mechanisms for operations and maintenance. The LGCDPs will be supported through formal training provided by CFAD, and will include targeted courses that will be developed and introduced by CFAD as the need presents itself over the course of Program implementation. In addition the LGCDPs will be supported by a system of "just-in-time" technical assistance to assist the LGs in developing the capacity to handle those key functions that are considered core to the effective operation of sound local Government, and which will be central to the PA system. These LGCDPs will include the LG's estimates of its needs for such technical assistance, but the "just-in-time" system will also be designed to respond quickly to demands as they arise, even if not anticipated in the LG's LGCDP. The just-in-time program will be managed by the regional offices of the Caisse, supported with consultancy contracts with firms that will be structured around the principle of providing expertise as needed.

45. The Program will also support the introduction of several initiatives that will focus on those central institutions and systems that have significant roles in the effective operation of LG in Tunisia, and which will strengthen the Government's decentralization, participatory governance and transparency agenda as established under the new Constitution. This will include support for: (i) the design and launch of a new

e-Portal (*Portail des Collectivités Locales*) which will make budget, procurement and audit information for all LGs as well as the results of LG performance assessments accessible to the public (and progressively, the E-Portal will also host LGs' information on Participatory Planning and Participatory Budgeting processes), (ii) the expansion of the Court of Auditors (*Cour des Comptes*)' annual LG financial auditing function to increase annual coverage so that by the end of the Program 80 percent of financial accounts legally received by the Court of Auditors (*Cour des Comptes*) from the LGs are being audited annually; (iii) the introduction and operationalization of the annual PA, to be undertaken by the *Contrôleur Général des Services Publics (CGSP)*; and (iv) the delivery of a series of nation-wide workshops by CFAD with assistance from DGCPL and CPSCL to introduce and familiarize the LG system (LGs, relevant institutions and Government agencies, and the general public) with the Program and PA process. Table 1.3 summarizes the capacity building arrangements under the Program.

Table 1.3: Capacity Building Arrangements under the Program

Area of Support	Description	Responsibility	Timing
Formal LG Training	Formal training programs addressing the functioning of decentralization systems and the operational responsibilities of LGs, for both elected officials and staff;	CFAD	Formal system already operational
Technical Assistance to LGs	Program of on-the job, just-in-time assistance provided to LGs on a demand-driven basis. Designed around principle of "learning by doing" and structured to provide expertise in key areas of LG need (finance, technical/engineering; social/citizen participation/accountability; fiduciary)	Caisse with assistance of CFAD and DGCPL	Offers opportunity of quick impact and "early wins". Should be fully operational in time for start of 2015.
Targeted Initiatives to Strengthen LG System	• Systematization of LG financial auditing of LGs • Introduction and operationalization of Performance Assessment (PA) System • Introduction of E-Portal to improve access to information to enhance LG accountability to citizens, and to strengthen DGCPL oversight (M&E) • Nation-wide workshops to introduce and familiarize LG system with Program and PA system • Targeted training for LGs (proc, safeguards, other – as needed)	• Cour Des Comptes • CGSP or CGF • DGCPL • CFAD • CFAD	• 2015 • 2016 • 2015 • 2014 • 2015

46. The program will also support the introduction of several initiatives which will support the Government's decentralization, participatory governance and transparency agenda as established under the new Constitution. Program initiatives will include the following:

47. **Participatory Planning**. The Program will support the introduction of participatory planning in all 264 municipalities beginning in the first year. Participatory planning will be a Minimum Mandatory Condition for the Program. The Participatory Planning approach will strengthen citizens' engagement with their municipalities on capital investments and enhance local accountability and transparency. The approach introduces requirements that LGs present the proposed five-year and annual investment plans and associated budgets with residents in public Town Halls for discussion and input. LGs are required to obtain resident validation of the proposed Plan, or on a modified form of the plan in the town hall meeting. The validated form of the plan will then be publicly disseminated in a variety of media. Capacity building and just-in-time support will be provided to LGs in preparing for and implementing the participatory planning process, including, importantly, on participatory planning, communications strategies, organization of public Town Hall meetings, and mediation.

48. **Participatory Budgeting.** Participatory budgeting works to increase citizens' engagement with their Governments and introduces them to the principles of public decision-making and budgeting. The Program will support the design and adoption of a participatory budgeting initiative beginning the first year of the Program, at which point LGs may choose to introduce the approach. Given many LGs' interest in strengthening citizens' engagement, it is anticipated that a fair number will adopt participatory

planning in the early years of the Program. As of year 4, however, the Performance Criteria will work to encourage widespread adoption of participatory budgeting. The participatory budgeting initiative will provide a strong incentive for residents to engage with their LGs since it permits them to directly decide how to spend a portion of the capital grant. LGs adopting participatory budgeting will be required to earmark five percent of their annual allocated capital investment grant for small-scale infrastructure projects proposed by residents and local civil society groups. All residents will be eligible to develop project proposals following pre-established Guidelines and Proposal Templates. The Guidelines will make it clear that proposals supporting gender-sensitive community infrastructure will receive additional weighting. All Proposals complying with the Guidelines will qualify to be presented at in an open public assembly where attendees will cast votes for their selected project proposals. Proposals receiving the most votes will be selected for implementation, up to the five percent budget envelope. The LG is responsible for implementing the selected proposals.

49. **Access to Information.** The Program will support the design and launch of a new E-Portal (*Portail des Collectivites Locales*) which will make budget, procurement and audit information for all LGs accessible to the public. Progressively, the E-Portal will also host LGs' information on participatory planning and participatory budgeting processes.

Program beneficiaries

50. The primary beneficiaries are the 264 municipalities and their seven million urban citizens (or 2/3 of the country total population). They will benefit from an enhanced inter-governmental transfers and from demand driven institutional and capacity development activities which will strengthen their capacity to deliver municipal infrastructure and services efficiently and consistent with their citizens' priorities. They will also benefit from initiatives to build knowledge and capacity of municipal council members and municipal staff on participatory governance initiatives which will underpin broader efforts to strengthen municipal efficiency and build a social contract between citizens and LG. The participation of local communities including, importantly, women and youth, in planning development activities managed by the municipality at the local level will ensure that vulnerable groups' needs are addressed, further fostering ownership and contributing to long term sustainability.

51. The secondary beneficiaries are targeted people living in underserviced/disadvantaged neighborhoods (more than 500,000 inhabitants in 229 neighborhoods). The main benefits will come from improved access to municipal services, overall improved municipal management and direct involvement of the population in setting investment priorities, and hence will have better living conditions. Investments activities financed with project funds will benefit this entire target group either directly or indirectly, including through creation of temporary employment which is likely to benefit youth particularly.

Program financing

52. The total outlay of Program and the Government indicative allocations among the three Program elements are presented in the table below. The IBRD loan of US$ 300 million represent about 83 percent of the total cost of the Program (US$363 million).

Table 4: Program Elements

	Amount (TND Million)	Amount (US$ Million)[22]
Capital Grant for Municipal Infrastructure Delivery	305	203
Capital Grant for improving municipal infrastructure in disadvantaged neighborhoods	225	150
Capacity support for improved LG institutional development	15	10
Total Program Financing	**545**	**363**

III Institutional Arrangements

53. Taking into account the fiscal nature of the reforms introduced under the Program, the Ministry of Economy and Finance (MoEF) is responsible for the Program and consequently the activities under the Program are financed directly by the MoEF through its annual budget. The MoEF will be responsible for Program implementation and for all transfer of funds under the Program. This will include ensuring that Program resources are budgeted for and disbursed within the Program expenditure framework according to existing state budget procedures.

54. An Inter-Ministerial Committee (IMC) was established on August 5, 2013 to oversee coordination of the Program, and is chaired by the Minister in charge of Local Governments within the Ministry of Interior (MoI).[23.] The IMC meets bi-annually (plus exceptionally as needed), providing strategic leadership and general direction for overall implementation of the Program. It is supported by the DGCPL, which will serve as the Secretariat to the IMC. The IMC will be responsible for sectoral coordination and for providing strategic leadership and general direction for the overall implementation of the Program.

55. The CPSCL is mandated under the Decree and according to the Law no. 37 dated May 14, 1975 to administer the capital grant transfers to the LGs. The process of the Capital Grant transfers will be detailed in the Program Operations Manual. The CPSCL will be responsible for coordination of day-to-day implementation of the Program and to facilitate the timely completion of inter-dependent functions to be performed by the several supporting agencies. Its responsibilities and functions in this regard, as well as those of the supporting agencies and the LGs will be detailed in the Program Operations Manual.

56. The CPSCL will be directly responsible, through its regional offices, for the execution of the technical assistance (just-in-time support) activities of the capacity building program (as described above).

57. The CPSCL will be responsible for: (i) day-to-day monitoring of implementation progress of the Program; (ii) Program reporting, including the annual midyear report and Program Progress Report; and (iii) preparing the Program Financial Statements, compiling them from municipal financial reporting, as well as from the financial reporting of the other supporting agencies.

[22] Exchange rate: 1USD = 1.50 TND
[23] Membership of the IMC includes representatives from the following ministries and Governmental agencies: (i) Interior, (iii) Finance, (iv) Regional Development, (v) CPSCL, (vi) CFAD, (FNVT) and (vii) ARRU.

58. The other national entities that will have guiding and supporting roles in the Program include: the Court of Auditors (*Cour des Comptes*), especially for the annual program audits and the annual external audit of municipalities; the Public Procurement Oversight Committee (*Haute Instance de la Commande Publique*,HICOP) which provides overall technical guidance on public procurement and monitors the compliance of procurement standards and practices; the Market Monitoring Committee (*Comité de Suivi et d'Enquete sur les Marchés*,COSEM) which receives complaints relating to public procurement and takes follow up action; the Controller General of Public Services (*Contrôleur Général des Services Publics*, CGSP) which will be in charge of the annual and independent PA the of LGs;. and the National Authority for Fighting Corruption ("*Instance Nationale de Lutte contre la Corruption*") which will be responsible for the investigation of complaints, if any, on fraud and corruption relating to the Program.

59. At the local level, LGs will plan and implement investments financed under the Program, building on the well-established systems and procedures developed during the last 20 years with support from the three previous Bank's funded Municipal Development Projects. As these LGs are the project owners for individual investment projects, funding from the grants will be reflected in the revenues and expenditures of the LG annual budgets. The LG will prepare the annual municipal investment plan for the Program, consolidated with the annual budget plan of the LG. The annual budget is discussed and approved by the municipal council and the annual municipal investment plan and the annual budget will be disclosed after adoption. The LG will be responsible for approval of feasibility studies and basic designs, detailed designs and cost estimates and procurement plans.

60. The LGs will ensure that their technical and administrative departments are adequately staffed and resourced and will outsource the supervision of their sub-project implementation to private or public entities when needed. Financial management, procurement and environmental and social management activities will be undertaken by LGs in accordance with enhanced Government procurement rules and procedures, including the preparation of : (i) annual investment plan; (ii) consultancy services terms of reference; (iii) feasibility studies, including necessary social and environmental impact assessments; (iv) detailed designs and cost estimates; (v) tender documents and (vi) the annual procurement plan. LGs will also be responsible for: (i) all procurement actions including advertising, bid evaluation and award of contracts, (ii) contract administration and management; (iii) technical supervision; (iv) verification of contractor's claims for payment, and issuing payment instructions to the municipal treasury (*Receveur municipal)*; (v) monitoring and proper reporting of physical progress of investments and (vi) ensuring assets are entered in the asset register of the LG on commissioning.

61. Municipalities require a wide range of expertise to successfully carry out their mandates. An analysis of staffing carried out as part of Program preparation reveals that most municipalities have the necessary staff, but all LG are expected to have the necessary support from DGCPL, CFAD and CPSCL and consulting firms, as LGs that do not meet this minimum condition will not be able to access Program funds.

IV Results Monitoring and Evaluation

62. The Results Framework (Annex 3) provides the basis on which the CPSCL, in close coordination with the LGs and supporting agencies, will appropriately measure and report on progress.

63. CPSCL will prepare Program consolidated Program performance and financial reports annually, as outlined in the Results Monitoring and Evaluation framework. The Program Progress Report will include consolidated financial statements that will cover all Program activities, expenditures and sources of funds, implementation status, progress in achieving the DLIs, result indictors, and evidence of

compliance with requirements of the Program Action Plan. The Program Operations Manual will include the format and details of reporting.

Annex 2: Results Framework Matrix

	Tunisia Urban Development and Local Governance Program – Results Framework												
Indicator	**Core**	**DLI**	**Unit of Measure**	**Base-line**	**2014**	**2015**	**2016**	**2017**	**2018**	**2019**	**Freq-uency**	**Method**	**Respo-nsibility for Data Collecti-on**
	The objectives of the Program are: (i) to strengthen Local Governments' performance to deliver municipal infrastructure, and (ii) to improve access to services in targeted disadvantaged neighborhoods.												
	PDO Level Results Indicators												
Percentage LGs that achieve at least 70% score in their annual performance assessment [24]	☐	☒	%	0	N/A	N/A	N/A	50	60	70	Annual	PA	CPSCL, CGSP
People living in targeted disadvantaged areas benefiting from improved municipal infrastructure (disaggregated by gender)	☐	☐	Number	0	0	0	00	150,000	300,000	500,000	Annual	LG Progress Reports PPR	LG, CPSCL
Number of Direct Beneficiaries of which 50% women	☒	☐	Number	0	0	7,000,000	7,000,000	7,000,000	7,000,000	7,000,000	Annual	LG Progress Reports PPR	LG, CPSCL
	Intermediate Results Indicators												
	Result Area 1: Capital Grant System reformed												
Capital grant system restructured through the amendment of	☐	☒	Yes/No	No	Yes	N/A	N/A	N/A	N/A	N/A	Once	Amended Decree published in the Official	MoI

[24] Performance areas include: Governance, sustainability and management.

Decree 97-1135												Gazette	
Timely publication of indicative unconditional capital grant allocation for each LG	☐	☒	Yes/No	No	No	Yes	Yes	Yes	Yes	Yes	Annual	E-portal and/or website	DGCPL, CPSCL
LGs that satisfy Minimum Mandatory Conditions (MMCs) and receive capital grants	☐	☒	%	0	N/A	60	70	80	90	90	Annual	Independent verification report	CPSCL, Verification Entity
	Results Area 2: LG institutional performance improved to deliver municipal infrastructures and services												
Independent LG performance assessment system introduced and threshold targets met.	☐	☒	Yes/No	None	No	No	No	Yes	Yes	Yes	Annual	Program performance report	CPSCL
LGs that have executed their Annual Investment Plans on schedule in terms of expenditures	☐	☒	%	35	N/A	40	50	60	70	80	Annual	Program performance report	CPSCL
LGs that received Capacity Building Support in accordance with their annual capacity development plan	☐	☒	Number	0	N/A	50	60	70	80	80	Annual	Program performance report	CPSCL, CFAD
Information on fiscal transfer and LG performance is publicly	☐	☐	Yes/No	None	No	No	No	Yes	Yes	Yes	Annual	E-portal	DGCPL

accessible														
	Results Area 3: Access to municipal infrastructure in targeted disadvantaged areas improved													
LGs that implement their investment plans for targeted disadvantaged neighborhoods according to schedule	☐	☐	%	0	0	0	30	60	80	100	Annual	Program performance report	LG, CPSCL	
People in urban areas provided with access to all-season roads within a 500 meter range under the program[25]	☒	☐	Number	0	-	-	-	-	-	-	Annual	Program performance report	LG, CPSCL	
People in urban areas provided with access to regular solid waste collection under the program	☒	☐	Number	0	-	-	-	-	-	-	Annual	Program performance report	LG, CPSCL	

[25] Targets to be established once the neighborhood upgrading programs are selected.

Annex 3: Disbursement Linked Indicators, Disbursement Arrangements and Verification Protocols

Tunisia Urban Development and Local Governance Program

Table 1: Disbursement Linked Indicators

DLI	Total DLI Allocation (Million US$)	As % of Total Financing Amount	DLI Baseline	Timeline for DLI achievement					
				2014	2015	2016	2017	2018	2019
Reform of the Capital Grant System									
DLI 1 The Government has replaced Decree No 97-1135 and restructured its capital grant system accordingly	30	10%	None	Yes	N/A	N/A	N/A	N/A	N/A
Allocated amount for DLI 1				*30*	*0*	*0*	*0*	*0*	*0*
DLI 2 Timely communication to LGs of the indicative Capital Block Grants (CBGs) allocation and timely transfer of CBGs to eligible LGs by the Government	20	6.7%	None	N/A	Yes	Yes	Yes	Yes	Yes
Allocated amount for DLI 2				*0*	*4*	*4*	*4*	*4*	*4*

Strengthened Local Government Institutional Performance and Municipal Infrastructure Delivery									
DLI 3 Acceptable percentage of LGs have met the MMCs and received CBGs	30	10%	0	N/A	60%	70%	80%	90%	90%
Allocated amount for DLI 3				*0*	*6*	*6*	*6*	*6*	*6*
DLI 4 The Government has designed and implemented an independent LG performance assessment (PA) system and required percentage of LGs have met the threshold PA scores	90	30%	None	N/A	Performance Assessment Manual adopted by Circular of the Minister of Interior	Performance Assessment Dry Run	50% of LGs achieve threshold PA scores	60% of LGs achieve threshold PA scores	N/A
Allocated amount for DLI 4				*0*	*20*	*20*	*25*	*25*	*0*
DLI 5 Required percentage of LGs have executed their Annual Investment Plans on schedule in terms of expenditures	45	15%	None	N/A	40%	50%	60%	70%	80%
Allocated amount for DLI 5				*0*	*5*	*10*	*10*	*10*	*10*
DLI 6 Required percentage of LGs have received capacity building support in	25	8.3%	None	N/A	50%	60%	70%	80%	N/A

accordance with their annual capacity development plan									
Allocated amount for DLI 6				*0*	*5*	*5*	*10*	*5*	*0*

Improved access to municipal infrastructure in disadvantaged neighborhoods									
				Disbursement from the Bank for DLI 7 will be calculated based on milestones reached on individual sub-projects. The schedule for achieving milestones and corresponding disbursement below are indicative only.					
DLI 7 Targeted number of people living in targeted disadvantaged neighborhoods have benefited from improved municipal infrastructure	40	13.3%	0%	N/A	Works contracts tendered are covering 20% of the target population	Works Contracts tendered are covering 50% of targeted population	Works Contracts tendered are covering 85% of targeted population Works Contracts covering 30% of targeted population are completed	Works Contracts tendered are covering 100% of targeted population Works Contracts covering 60% of targeted population are completed	Works Contracts covering 100% of targeted population are completed
Allocated amount for DLI 7				*0*	*1.6*	*2.4*	*12.4*	*10.8*	*12.8*
Strengthening of Local Government Systems									
DLI 8 Transparency and access to information improved	20	6.7%		N/A	E-portal hosted by the DGCPL designed and operational	At least 60% of LG annual financial accounts legally received by the Cour des Comptes are audited by September 30	At least 70% of LG annual financial accounts legally received by the Cour des Comptes are audited by September 30	At least 80% of LG annual financial accounts legally received by the Cour des Comptes are audited by September 30	N/A

						of current year	of current year	of current year	
Allocated amount for DLI 8				*0*	*10*	*3*	*3*	*4*	*0*

Table 2: DLI Verification Protocol

DLI	Definition/ Description of achievement	Scalability (Yes/No)	Protocol to evaluate achievement of the DLI and data/result verification		
			Data source / agency	**Verification Entity**	**Procedure**
DLI 1 The Government has replaced Decree No 97-1135 and restructured its capital grant system accordingly	By Program effectiveness, Decree 97-1135 amended to reflect the core elements of the capital grant reform incl. introduction of the formula based allocation; timely publication and transfer of annual allocation; use of capital grant at the discretion of LG, progressive implementation of annual and independent LG performance assessment	No	MoEF	Bank with support from IVA	Submission to the Bank of approved decree reflecting the core elements of the CGS reform and its publication on the Official Gazette.
DLI2 Timely communication to LGs of the indicative Capital Block Grants (CBGs) allocation and timely transfer of CBGs to eligible LGs by the Government	From Program year 2 onwards, Annual allocation of CBGs published no later than Dec 1 of the preceding year and disbursed no later than Feb 1 of the current year	No	CPSCL	Bank with support from IVA	From Program year 2, the CPSCL will notify the Bank of the date and means of publication of the annual allocation and will submit the documentation relative to the disbursements. Verification by the Bank with support from the IVA that the annual allocation is consistent with the provisions of the decree, that the indicative annual allocation of capital block grants has been timely communicated to LGs to use the information for the preparation of their annual investment plan, and that the disbursements have been completed by the target date to eligible LGs.

DLI 3 Acceptable percentage of LGs have met the MMCs and received CBGs	Annual targets are defined in terms of percentage of LGs meeting the MMCs. The Annual targets are : CY 2015 : 60% of LGs CY 2016 : 70% of LGs CY 2017 : 80 % of LGs CY 2018 : 90% of LGs CY 2019 : 90% of LGs	Yes	LGs and CPSCL / PA	Bank with support from IVA	Each year, the LGs will communicate to the CPSCL the documentation relative to the satisfaction of MCC. In the first and the second year of the Program, the CPSCL will review the documentation and determine the compliance of each municipal investment plan with the provision of the Ministerial Decree. Starting from the third year, this review will be fully integrated to the annual performance assessment of LGs to be carried out by the independent entity. The assessment report and supporting documentation will be made available by the CPSCL for the Bank with support from the IVA to carry out a sample audit.
DLI 4 The Government has designed and implemented an independent LG performance assessment (PA) system and required percentage of LGs have met the threshold PA scores	In CY 2015: The PA system is developed and the PA manual is adopted by MoI In CY 2016: the PA system is tested and implemented. In CY2017 50% of LGs achieve threshold PA scores In CY 2018: 60% of LGs achieve threshold PA scores	Yes	CPSCL / PA	Bank with support from IVA	The entity in charge of PA will provide to the Bank through the CPSCL the supporting documentation relative to the achievement of targets for CY 2015, and 2016, and the Performance assessment reports for CY 2017 and 2018
DLI 5 Required percentage of LGs have executed their Annual Investment Plans on schedule in terms of expenditures	Percentage of LGs which have executed at least 70% of the expenditures involved in their annual investment plan. The annual targets are CY 2015 : 40 % of LGs CY 2016 : 50 % of LGs CY 2017 : 60 % of LGs CY 2018 : 70 % of LGs CY 2019 : 80 % of LGs	Yes	CPSCL/PA	Bank with support from IVA	Each year, the LGs will prepare a progress report on the execution of their investment budget. The CPSCL will compile the progress reports in a consolidated progress report for the same year. The Bank with support from the IVA will verify the achievement of the target through sample audits.
DLI 6 Required percentage of LGs have received capacity building	Annual targets are defined in terms of percentage of LGs which have preparedand substantially executed a Capacity Development	Yes	LG / CPSCL / CFAD	Bank with support from IVA	Starting from CY 2015, each LG prepares and executes with the support of the CPSCL and CFAD an Annual Capacity Development Plan (ACDP)

support in accordance with their annual capacity development plan	Plan. The Annual targets are : CY 2015 : 50% of LGs CY 2016 : 60% of LGs CY 2017 : 70 % of LGs CY 2018 : 80% of LGs				covering the same areas covered under the PA. Each LG transmits its final ACDP to the CPSCL by February 15th of the current year. Each LG submits to the CPSCL a progress report on the execution of its ACDP by February 1st of the following year. The CPSCL will submit a consolidated report on the implementation of the LGs' ACDPs for the previous year to the IVA by March 15th of each year. The Bank with support from the IVA will verify the achievement of the target.
DLI 7 Targeted number of people living in targeted disadvantaged neighborhoods have benefited from improved municipal infrastructure.	This is defined as the percentage of the target population for which works contracts have been signed and completed.	Yes	CPSCL	Bank with support from IVA	Each year, the LGs will prepare a physical progress report on investments funded as part of the Program. In addition, the LGs will make available to the CPSCL all documentation relative to each subproject's compliance with the Program's provision on (i) sub-project's eligibility, (ii) feasibility studies, (iii) procurement, (iv) environmental and social management, and (v) inclusion of the assets created in the LG municipal asset management system. The CPSCL will review the documentation and determine the compliance of each municipal investment. The CPSCL will submit to the Bank a consolidated report on progress and compliance of the investment sub-projects in targeted neighborhoods. The assessment report and supporting documentation will be made available by the CPSCL for the Bank with support from the IVA to carry out a sample audit.
DLI 8 Transparency and access to information improved	In CY 2015, the E-portal is designed and operational. From CY 2016, annual targets in terms of timely completion (by Sep 30 of the current year) of audits of the financial statements	Yes	DGPCL & Cour des Comptes	Bank with support from IVA	In CY 2015, the DGPCL will submit the final approved design of the E-Portal and a progress report on its operationalization to the Bank through the CPSCL. The Bank with support from the IVA will verify the achievement of the corresponding targets. For CY 2016, 2017, and 2018, the Bank with support

	received from the LGs are met.				from the IVA will refer to the audit reports published by the Cour des Comptes and will verify the achievement of the corresponding targets.

Table 3: Bank Disbursement

DLI	Bank financing allocated to the DLI	Of which Financing available for		Deadline for DLI Achievement[1]	Minimum DLI value to be achieved to trigger disbursements of Bank Financing [2]	Maximum DLI value(s) expected to be achieved for Bank disbursements purposes [3]	Determination of Financing Amount to be disbursed against achieved and verified DLI value(s) [4]
		Prior results	Advances				
DLI 1 The Government has replaced Decree No 97-1135 and restructured its capital grant system accordingly	30	30	-	Program effectiveness	N/A	N/A	Yes/No. This is a prior result and disbursement will take place upon program effectiveness.
DLI 2 Timely communication to LGs of the indicative Capital Block Grants (CBGs) allocation and timely transfer of CBGs to eligible LGs by the Government	20	0	0	July 15 of each year for communication of annual allocation. March 1st of each year for grant transfer	N/A	N/A	Yes/No. The sub indicator for each year must be verified in full for the disbursement to occur. If the target is not met for a given year, the undisbursed amount will be redistributed equally in the projected disbursement of next years.
DLI 3 Acceptable percentage of LGs have met the MMCs and received CBGs	30	0		December 31st of each year.	30%	CY 2015 : 60 % CY 2016 : 70 % CY 2017 : 80 % CY 2018 : 90 % CY 2019 : 90 %	The achievement of this DLI will be assessed every year for each LG on a Pass/Fail basis. Disbursement from the Bank will proportionate to the number of LG achieving the DLI. D=A*(C/T)/G *Where:* D= annual disbursement A= annual allocation C= number of LGs compliant T= total number of LGs

							G= annual goal in percentage (*)= multiplied (/)= divided (>)= greater than (<)= lesser than If C/T < 0.3, D = 0 If C/T > G, D=A If the target is not met for a given year, the undisbursed amount will be redistributed equally in the projected disbursement of the following years.
DLI 4 The Government has designed and implemented an independent LG performance assessment (PA) system and required percentage of LGs have met the threshold PA scores	90	0	0	December 31st of each year.	N/A for the first three year. For CY 2017 and 2018: 15%	N/A for the first three years CY 2017: 50% CY2018: 60%	Amount allocated for CY2015, and 2016 targets will be disbursed on a yes/No basis. The sub indicator for each year must be verified in full for the disbursement to occur. If the target is not met for a given year, the undisbursed amount will be disbursed in the next years, when the target is met. For CY 2017 and 2018 disbursement from the Bank will be determined by the number of LG achieving the threshold PA score as a result of their Annual Performance Assessment. D=A*(C/T)/G Where: D= annual disbursement A= annual allocation C= number of LGs compliant T= total number of LGs G= annual goal in percentage (*)= multiplied (/)= divided (>)= greater than (<)= lesser than

							If C/T < 0.5, D = 0 If C/T > G, D=A If the target is not met for a given year, the undisbursed amount will be redistributed equally in the projected disbursement of next years
DLI 5 Required percentage of LGs have implemented their annual investment plans on schedule	45	0	30	December 31st of each year.	15%	CY 2015 : 40 % CY 2016 : 50 % CY 2017 : 60 % CY 2018 : 70 % CY 2019 : 80 %	Achievement of the DLI objective of at least 70% implementation of the annual investment plan will be assessed on a Yes/No basis for each LG and disbursement will be proportional to the percentage of LGs passing against the annual target. D=A*(C/T)/G Where: D= annual disbursement A= annual allocation C= number of LGs compliant T= total number of LGs G= annual goal in percentage (*)= multiplied (/)= divided (>)= greater than (<)= lesser than If C/T < 0.15, D = 0 If C/T > G, D=A If the target is not met for a given year, the undisbursed amount will be redistributed equally in the projected disbursement of next years.
DLI 6 Required percentage of LGs have received	25	0	0	December 31st of each year.	15%	CY 2015 : 50 % CY 2016 : 60 % CY 2017 : 70 %	For Program years 2, 3, 4, and 5 targets, the achievement of this DLI will be assessed every year for each LG on a Yes/No basis. The DLI will be achieved for each LG if

capacity building support in accordance with their annual capacity development plan						CY 2018 : 80 %	70% of the capacity building plan has been completed. Disbursement from the Bank will proportionate to the % of LG achieving the DLI. D=A*C/T *Where:* D= annual disbursement A= annual allocation C= number of LGs compliant T= total number of LGs G= annual goal in percentage (*)= multiplied (/)= divided (>)= greater than (<)= lesser than If C/T < 0.15, D = 0 If C/T > yearly target, D=A If the target is not met for a given year, the undisbursed amount will be redistributed equally in the projected disbursement of next years.
DLI 7 Targeted number of people living in targeted disadvantaged neighborhoods have benefited from improved municipal infrastructure	40	0	30	December 31st of each year.	>20,000	500,000	Disbursement from the Bank will be calculated based on milestones reached on individual sub-projects. D=Ps*0.2*U+Pc*0.8*U *Where:* D= total disbursement Ps= Sum of population in disadvantaged neighborhoods for which the contracts have been tendered Pc= Sum of population in disadvantaged neighborhoods for which the works have been completed U= A/Pt A= total allocation Pt= total target population in

							disadvantaged neighborhoods
							(*)= multiplied
							(/)= divided
							(>)= greater than
							(<)= lesser than
							
							If (Ps*0.2)+(Pc*0.8)<20,000, D=0
							
							If (Ps*0.2)+(Pc*0.8)> Pt, D=A.

DLI8: Transparency and access to information improved	20	0	0	December 31st of each year.	30%	CY 2016 : 60 % CY 2017 : 70 % CY 2018 : 80 %	Disbursement for CY 2015 allocation on a Yes/No basis. Disbursements for CY 2016, 2017, and 2018 D=A*(K/T)/G *Where:* D = Annual disbursement A= Annual allocation K = Number of annual Audits completed by Sep 30 of each year T = Total Number of LG financial statement legally submitted by LG to the Cour des Comptes G = Annual goal (expressed in percentage of audits completed) (*)= multiplied (/)= divided (>)= greater than (<)= lesser than If K/T < 0.3, D = 0 If K/T > G, D=A If the target is not met for a given year, the undisbursed amount will be redistributed equally in the projected disbursement of next years.

Annex 4: Technical Assessment Summary

I. Program Strategic relevance

1. In response to the Revolution of 2011, Tunisia has sought to introduce policies that firmly ground voice and accountability into the governance structure of the country. To this end the new, recently adopted Constitution embeds decentralization as a cornerstone of its strategy to bring Government closer to its citizens. This requires transformational changes to the operating framework of LG, and the Program is designed to support key reforms necessary to restructure the institutional and fiscal architecture to more effectively address the decentralization provisions contained in the Constitution. The reforms pose several challenges to the existing structures of LGs, most notably, in light of the greater municipal autonomy mandated in the Constitution, the need to: strengthen LGs to be better able to perform their essential functions of citizen consultation and accountable service delivery independently of central intervention; revamp the existing oversight system (*"tutelle"*) from one of central Government controls, clearances and approvals for local investment decision-making, to one of central support, capacity strengthening and policy reform for LGs to be better able to undertake their mandates; and address several key provisions of current regulatory requirements in the operation of LGs, particularly regarding the system of Inter-Governmental Fiscal Transfers, that have proven counter-productive and have fostered outcomes contrary to those intended by the policies in place.

2. **The Program design consequently has high strategic relevance for Tunisia's development.** It is calibrated to introduce the reforms in a manner recognizing: (a) that the transition to an effectively functioning decentralization system of fully-devolved LG will take time; (b) that builds on existing systems, taking advantage of existing strengths; and (c) the changes to the fiscal architecture and regulatory framework necessary to directly translate the Constitutional mandate into practice in areas that offer prospects for early wins and establish the core elements of viable and accountable local governance. The restructuring therefore is carefully sequenced to focus on those actions that, on the one hand will have transformative consequences, and introduce sustainable systems and practices, while on the other hand are phased in, according to graduated reforms that are practical and can be implemented in the short term to have immediate impact on addressing key provisions under the Constitution.

3. **Analysis of existing regulatory systems and procedures, and institutional structures suggests that reforms to the capital grants will introduce significant advances towards accountable local governance and better capacitated local Governments, constituting an effective first phase of the broader decentralization agenda established under the Constitution**. The Program therefore will operate within the existing fiscal architecture by restructuring the existing capital grant window for transferring resources to municipalities from a system that is regulated by centrally determined and opaque allocation procedures and investment priorities, into a window regulated by a system of resource transfers made according to: (a) a formula based unconditional capital grant system for uses determined fully at the discretion of the LGs; and (b) a conditional grant system managed by the LGs but for investment purposes deemed to be national policy priorities.

4. The formula based unconditional grant system is designed to address the following issues considered central to meeting the mandate of the new Constitution: (a) allocative equity, objectivity, and transparency; (b) greater voice for citizens in the operational and service delivery responsibilities of their local Governments through: (i) citizen consultation by local Governments in the use of the discretionary grant funds, and (ii) increased accountability of the local Governments to their citizens through timely access to relevant information about local Government performance; and (c) effective incentives through grant access requirements that encourage LGs to perform better along key parameters essential to enhancing their accountability to their citizens and strengthening their planning, fiduciary and operating capabilities on an ex post rather than the ex-ante *"tutelle"* system.

5. In order to capture these reforms, Program preparation and implementation supports the revision and operationalization of Decree 97-1135 that governs and regulates the fiscal system for LG in the country. It also is designed to underpin and function within the Government's well-established PIC system of resource transfers and LG service delivery. The Program also conforms to the World Banks' Country Interim Strategy Note (ISN) for Tunisia for 2013-2014. The ISN spells out a set of three broad areas for Bank engagement and, within those areas, a number of Driving Objectives that the Bank will pursue. The proposed operation is fully aligned with the ISN's second area of engagement: promoting social and economic inclusion. Within this second area, the operation addresses Driving Objective 5, improving access to basic services for under-served communities. About half a million people or eight percent of the urban population living in disadvantaged neighborhoods are targeted through the proposed program. The proposed operation is also in line with the ISN's third area of engagement: strengthening governance through voice, transparency and accountability. The operation's focus on local governance institutions, decentralization, and significantly strengthening participatory democracy at Local Government level directly supports this.

II. Technical soundness

6. **The Program development objective is to improve institutional performance of LGs in the context of Government's reform initiatives to establish fully decentralized LGs.** The Program is designed to meet this objective and is technically sound because it draws on international best practice and integrates it with the specific circumstances of the Tunisian reform initiative. In particular, consistent with the Government's policy of phasing its program of decentralization reform, the Program utilizes fiscal instruments to effectuate the initial round of reforms.

7. The Program conforms to principles core to operating an effective fiscal decentralization framework, including: a) Linking the transfer of grant resources to improvements in LG performance in those areas of LG operations considered as the most important functions for strengthening their institutional capabilities; and b) Operating within the existing fiscal architecture, regulatory regimes, and institutional systems.

8. The Program is built around two design elements that draw on international best practice, but is tailored to the policy reform environment in Tunisia: (a) All 264 entities that are formally designated as municipalities (LGs) in Tunisia will participate in the Program. The justification for this broadly inclusive approach is derived from the assessment that clearly demonstrates absorptive capacity of the LGs, management and administrative capacity of the CPSCL, soundness of the primary planning vehicle (the PIC), and the robustness of the key operating systems such as procurement practices. In addition, the size of the resource transfers will remain consistent with past allocation levels. Consequently, the delta will not be managing major grant increases, but adjusting to the reforms most notably: the change in responsibility and accountability for selecting and implementing investment choices, and improving essential operating capabilities. To this end, the performance system will be introduced incrementally, and there will be a significant augmentation of the capacity support system. And (b) the size of the unconditional capital grant has to be sufficient to incentivize LGs to seek access to it, and therefore to be motivated to improve their performance. While the size of the grants will only increase within the normal range that has characterized prior PIC increases, the incentives lie in three areas: they are the only capital development funds available to most LGs, and they are in the form of unconditional grants; they will now be available as entirely discretionary funds to the LGs, and their use will be fully determined by the LGs; the effectiveness of their use (and the ability of the LG to continue to access them) will be based on measurement by an independent agency, with the results made available to the citizens of each LG; and these funds are sufficient to allow for significant levels of investment in pressing local infrastructure priorities.

9. The design of the Program directly addresses key features of the existing system that either embed the *"tutelle"* system, or over time have had increasingly perverse effects (and all these features are incorporated into the revised Decree), including:

- **The system for allocating grants has not been transparent.** Under the Program, a formula has been introduced that is based on considerations of distributive equity (population has been used for this), and redistributive considerations as measured by fiscal capacity – a proxy for the strength of the economic base (poverty, social indicators, and unequal access to services were all considered, but data was poor). Data for the formula are derived from two independent sources – National Bureau of Statistics and Ministry of Finance) and are both measurable and objective. The formula assigns 80 percent to population and 20 percent to fiscal capacity, and Annex 1 details the allocations to each LG based on the formula.

- **Grant access requirements under the previous version of the Decree that linked the use of grant funds to requirement to utilize loan funds in predetermined ratios have led to serious levels of fiscal stress i**n nearly half the LGs. Under the reforms, these linkages have been terminated and the use of grant funds is subject only to council decisions on their investment priorities.

- **The prior linkage of grants to loans led to the well-endowed LGs being increasingly favored** as measured by the disproportionate per capita share of the grants they were able to garner, exacerbating regional disparities. The delinking combined with the allocation formula addresses this issue directly, while still allowing the better-off LGs access to the loan funds to the maximum extent of their capacity to borrow.

- **The grant system undermined accountability of LGs to their citizens.** With opaque allocation criteria and decisions on investment priorities taken at the center, there has been little basis for the LGs to engage with their citizens, and no basis for the citizens to hold their councilors accountable, except on the margin for operating and maintaining existing assets. In addition there was no effective system for measuring LG performance, and no means of providing citizens with useful and timely information on their LGs operations. Under the reforms, the objective and predictable flow of funds and the unfettered responsibility of the LGs to determine the use of the funds creates the space for consultation and accountability to be introduced and for social contracts to be built between LGs and their citizens. The introduction of performance standards LGs, together with systems for ensuring timely citizen access are also provided for in the Decree.

- **There has been no system for assessing and monitoring LG performance.** Under the Program of performance requirements linked to grant access is being introduced. The system will be phased and will start in year 1 with a set of Minimum Mandatory Conditions (MMCs) that will be enhanced each year until the third year when the MMCs will be retained, but will be augmented by an annual independent performance assessment. The findings will be published at the time of their completion each year and will be applied to the level of disbursement of the grant funds to each LG.

- **Weak capacity of the LGs undermines the effectiveness of the performance-based incentive system.** The Program has responded to this by providing for two areas of support. One is to strengthen existing curricula and training programs of CFAD, the agency established for delivering classroom-based training to LGs (elected officials and staff). The other is to establish cadres of technical experts in each of the CPSCL regional offices with resources to contract in skills on a just-in-time basis to respond to on-the-job capacity support to LGs dealing with issues of planning, budgeting, financial management, revenue generation, asset management, environmental and social safeguards, procurement issues.

10. Extensive discussions have been held with the key stakeholders involved in the decentralization agenda and the development of the program, including the policy agencies and the CPSCL, the implementing agency. In addition, the Program has been discussed with officials from a number of LGs and with the formal organization representing LG in Tunisia, as well as in meetings held with representatives from different LGs.

III. Implementation Arrangements

11. **Program Coordination and Monitoring.** The Program implementation, under the overall responsibility of the Ministry of Economy and Finance, will involve several Governmental entities with strong need for coordination. To the end, a national level Inter-Ministerial Committee (IMC) has been established by a Decision of the Minister of Interior in August 2013 to provide broad oversight of the Program and guidance for its proper implementation. The key role of the IMC is to provide strategic leadership and general direction for overall implementation of the Program. The IMC will be chaired by the Minister in charge of Local Government within the Ministry of Interior and will include high level representative of involved entities. The DGCPL will act as a Secretariat of the IMC[26] and will provide technical support to the IMC in preparing agendas and overseeing follow-up actions. The IMC meets bi-annually (plus exceptionally as needed).

12. The DGCPL in charge of developing municipal sector policies and strategies will play an important role during the mid-term review of the program and will recommend any adjustment needed to achieve the Program objectives and results. In addition, the DGCPL will host and manage the E-portal for Local Governments.

13. **Management of the Program.** The CPSCL has been designated to be responsible for coordination of day-to-day implementation of the Program and to facilitate the timely completion of inter-dependent functions to be performed by the Program's supporting agencies. The CPSCL has well established capacity for performing this functions as it has operated the PIC cycle and the grant and loan program for LGs in Tunisia for many years. As part of this coordination function, CPSCL will have responsibility for ensuring that the various elements of the Program are properly implemented according to schedule. In addition, CPSCL will have direct responsibility for managing the grant allocation process, per the provisions of the new decree, and will serve as a pass though for the flow of grant funds to the LGs. CPSCL will manage, through their regional offices, the on-the-job element of the capacity building program and ensure just in time technical assistance to LGs to enable them to meet the performance criteria required for accessing the grant funds. The CPSCL will ensure adequate reporting to the Bank on Program implementation progress.

14. The World Bank will transfer funds to the MoEF based on the submission of consolidated, verified information on the DLIs. MoEF will then be responsible for the financing of the Program activities and particularly the release of funds to the LGs through CPSCL. CPSCL will be responsible for managing the front end of the conditional and unconditional capital grant process according to the amended Decree 97-1135: (i) the PAs would be undertaken by the Controller General of Public Services (CGSP), and compiled into reports by July 1 of each year for review and sign off by the IMC and for publication on the e-portal and in the media; (ii) based on the allocation formula, and the

[26] Membership of the IMC includes representatives from the following ministries and Governmental agencies: (i) Interior, (iii) Finance, (iv) Regional Development, (v) CPSCL, (vi) CFAD, (FNVT) and (vii) ARRU.

application of the PA results by CPSCL and with confirmation in principle from the MoEF of indicative funding for the forthcoming year, CPSCL will inform each LG of its grant allocation for the forthcoming year no later than August 1 to meet the budgeting cycle of the LGs; (iii) the LG would then complete its budget preparation, which would include its investment plan, and adopt the budget by December 31; (iv) during the budget preparation period, the LGs would in parallel negotiate with CPSCL for any loans they may wish to include in their investment plans, and would follow CPSCL procedures to qualify; (v) the LG budgets would then be submitted to MoEF for confirmation of grant fund allocations; (vi) by December 31, the LGs would submit their MMCs compliance confirmation to the CPSCL for review and submission to the IMC for approval, prior to any funds being disbursed to the LGs; and (vii) the MoEF would release the grant funds through CPSCL into the Treasury-held local LG accounts , and CPSCL will be responsible for the separate release of the loans to the LGs to support the implementation of their municipal investment plans. The Court of Auditors (*Cour des Comptes*) will be responsible for conducting the annual Audit of the Program financial statements. .

15. **Implementation at municipal level.** The LGs will manage the core of the Program; they will be responsible for the planning and budgeting of their investments, and for their implementation. They will be responsible for maintaining the requisite records and reporting procedures regarding the use of the grants, and the implementation of their capacity development plans. They will also be responsible for taking the requisite actions to satisfy the MMCs and the Performance Assessments. An assessment of LG capacity indicates that they have a good track record in absorbing the level of grant funds proposed under the Program, that they have established some measure of capacity (including utilizing the local consulting sector) for undertaking requisite infrastructure investment pre-feasibility and preparatory studies as well as procurement and implementation supervision management. A recent assessment indicates, of the responses received, 175 out of the 264 have at least a *Technicien Supérieur* among their staff, of whom 91 are engineers.

16. The LGs will submit evidence according to a format set out in the Program Operations Manual that they have met the MMCs and a desk audit of all 264 submissions will be conducted by the CPSCL. They will similarly be responsible for preparing the requisite information, according to formats set out in the Performance Assessment Manual attached to the Program Operations Manual, necessary for the CGSP to be able to undertake the Performance Assessments when these are introduced. The CGSP will conduct desk reviews of all 264 assessments based on documentation submitted by the LGs, supplemented by field checks according to statistically valid random sampling methodology. The CGSP is well recognized for its high standards, experience in this area, and its independence.

17. LGs will plan and implement investments financed under the Program, building on the well-established systems and procedures developed during the last 20 years with support from the three previous Bank-funded Municipal Development Projects. As LGs are the project owners for individual investment projects, the funding from the grants will be reflected in the revenues and expenditures of the LG annual budgets. The LG will prepare the annual municipal investment plan for the Program, consolidated with the annual budget plan of the LG. The annual budget is discussed and approved by the Municipal Council and the annual budget, including the municipal investment plan will be disclosed after adoption. The LG will be responsible for approval of feasibility studies and basic designs, detailed designs and cost estimates and procurement plans.

18. LGs will ensure that their technical and administrative departments are adequately staffed and resourced and will outsource the supervision of their sub-project implementation to private or public entities when needed. Financial management, procurement and environmental and social management activities will be undertaken by LGs in accordance with enhanced Government procurement rules and procedures, including the preparation of: (i) the annual investment plan; (ii) consultancy services terms of reference; (iii) feasibility studies, including necessary social and environmental impact assessments; (iv)

detailed designs and cost estimates; (v) tender documents; and (vi) the annual procurement plan. LGs will also be responsible for: (i) all procurement actions including advertising, offer evaluation and award of contracts, (ii) contract administration and management; (iii) technical supervision; (iv) verification of contractor's claims for payment, and issuing payment instructions to the municipal treasury (*Receveur municipal)*; (v) monitoring and proper reporting of physical progress of investments; and (vi) ensuring assets are entered in the asset register of the LG on commissioning.

19. **Supporting Agency.** The Decentralization Support and Training Center *(Centre de Formation and Appui à la Decentralisation)* (CFAD) will be in charge of classroom-based training and the workshops to be held to familiarize the LGs and the central agencies with the Program activities and objectives. CFAD will be also in charge of developing and delivering additional training programs that target gaps in areas of LG responsibility that affect their performance and that may be identified during Program implementation, particularly those that emerge through the performance assessment system.

IV. Description and Assessment of Program Expenditure Framework

4.1 Review of the current system of financing municipal systems:

21. Infrastructure delivery in municipalities is currently financed by the central Government through a combination of budget financing, loans from CPSCL and own source revenues of municipalities. The central budget financing of local service delivery is through four channels;

(i) Capital Investment grants distributed through CPSCL;
(ii) Recurrent grants provided for meeting current expenditure distributed through the Common Fund for LG (*Fonds Commun*, FCCL);
(iii) Current or investment grants channeled through specific program (often towards regional councils) to support sector policies defined by sector ministries. Grants are then reflected in the sector ministry's budget; and
(iv) Indirect support, often in kind, when central Government manages tasks normally under the responsibility of LGs.

22. The Capital investment plans of Municipalities are funded out of the Government's capital budget (*Titre II*) and appear in the national budget under the budget head for the Ministry of Interior as transfers to the CPSCL (*Titre II, line 2.1*[27]). Municipal investments take place primarily within the framework of the following three programs or windows: (i) investments supported under the five-year Municipal Investment Plans (PIC), a form of grant that has some flexibility in the type of investments it supports and in the degree of choice the LGs can exercise; (ii) similar investments supported outside the five-year plan (*hors*-PIC); and (iii) investments supported under the national program for the rehabilitation of disadvantaged neighborhoods (PNRQP). There is a fourth category that provides funds for other types of investments not covered under the other programs, such as regional landfills.

23. The PIC has been operating for over thirty years in Tunisia and follows a central planning model whereby resources are agreed in principle by the MoEF for a five-year investment cycle and are locked in through investment plans prepared for each LG. While the LGs are consulted at the beginning of the cycle on their priorities, final decisions are taken though an inter-ministerial process, managed by the CPSCL, that largely excludes further input by the LGs, with final decisions rarely conforming to LG proposals. At the beginning of each CY, the Government contribution for the forthcoming year is

[27] See link http://www.finances.gov.tn/index.php?option=com_jdownloads&Itemid=712&view=finish&cid=537&catid=1&lang=fr p. 15 of the document

formally approved in the budget. Municipalities prepare five year investment plans and submit them to the MoEF and Ministry Interior for approval. The five-year plans comprise a list of capital investment projects that the municipality hopes to implement during the coming five years. Every year municipalities prepare an annual plan comprising of a list of projects chosen from the five year plan and submits them for funding from the PIC allocation. A Financing Committee comprising representatives from the Ministries of Economy and Finance, Interior, Development and Planning as well as the representative of CPSCL approves the proposals for funding and allocate the capital grants for each of the project so approved. Table 4.11 examines the PIC component of the capital budget over the past two PIC cycles, disaggregated into the three main sources of investment funds (own source revenues, loans and grants), and comparing them to the PIC cycle just commencing (2014-2019). The table also compares allocations with actual expenditures.

24. The PIC establishes a rigid framework that does not permit changes to the plan once it has been confirmed. Consequently, the "outside-PIC" window has arisen as a means of allowing for some investments to be funded as exceptions to the PIC, and these have to be approved on a case by case basis. The lack of flexibility in the PIC limits the LGs' ability to respond to changing circumstances and priorities, and has particular consequences for the existing status of the LG councils which comprise nominated Councilors with little local credibility. Local elections planned for 2015/16 will severely challenge fixed investment plans.

Table 4.1: Comparison of PIC allocations over three PIC cycles (2002 to 2019)[28]

Funding Source	PIC 2002-2006 (TDN '000,000)		PIC 2007-2011 (TDN '000,000)		PIC 2014-2019 (TDN '000,000)
	Projected	Utilized	Projected	Utilized	Projected
OSRs	170.8	124.2	179.1	121.0	193.0
Loans	302.4	257.5	306.0	260.5	389.0
Grants	209.2	214.6	261.1	267.0	305.0
Total	682.4	596.3	746.2	648.5	887.0

Source: CPSCL

25. The capital grants under the PIC are part of the financing mix of municipal capital investment plans that include their own source revenues as well as loans issued by CPSCL. This mix is framed by a decree (#97-1135, 16 June 1997) according to the nature of the investment project to be funded. The usual mix is (for small public works which represent the vast majority of projects) 37 percent loans, 33 percent grants and 30 percent self-financing, but studies for instance are funded only through grants and other types of investments have a different mix. Loans from CPSCL have an interest rate between 6 and 8.5 percent and are reimbursable between 7 to 15 years, with a first installment the second year.

Table 4.2: Aggregate Municipal Budgets 2002-2012

[28] Data sources show a small discrepancy in the CPSCL loan amounts between Tables 4 and 5 (about 3 percent).

Year	02	03	04	05	06	07	08	09	10	11	12
Recurrent revenues /T1	309	324	351	374	409	427	458	479	536	561	641
OSR	223	234	258	279	312	322	346	360	404	268	370
FCCL	86	90	92	95	98	105	112	119	131	145	176
Exceptional transfers	0	0	0	0	0	0	0	0	0	148	95
Recurrent Expenditure / T1	258	272	289	306	332	350	376	403	428	460	502
Capital resources / T2	160	137	166	166	154	159	170	235	246	218	228
Capital Expenditures / T2	154	130	166	160	149	141	132	188	194	140	129
Investments	129	98	135	126	115	101	89	144	146	87	59
Capital Reimbursement	25	32	31	34	34	40	43	45	48	54	60

Source : Municipal Finance Report, Sinet 2013

26. Table 4.2 presents a summary of municipal budgets over the 2002-2012 period. Nation-wide sector specific programs such as the PNRQP are implemented by a central agency (ARRU), which has also required LGs to utilize loan funds as part of their financing plan.

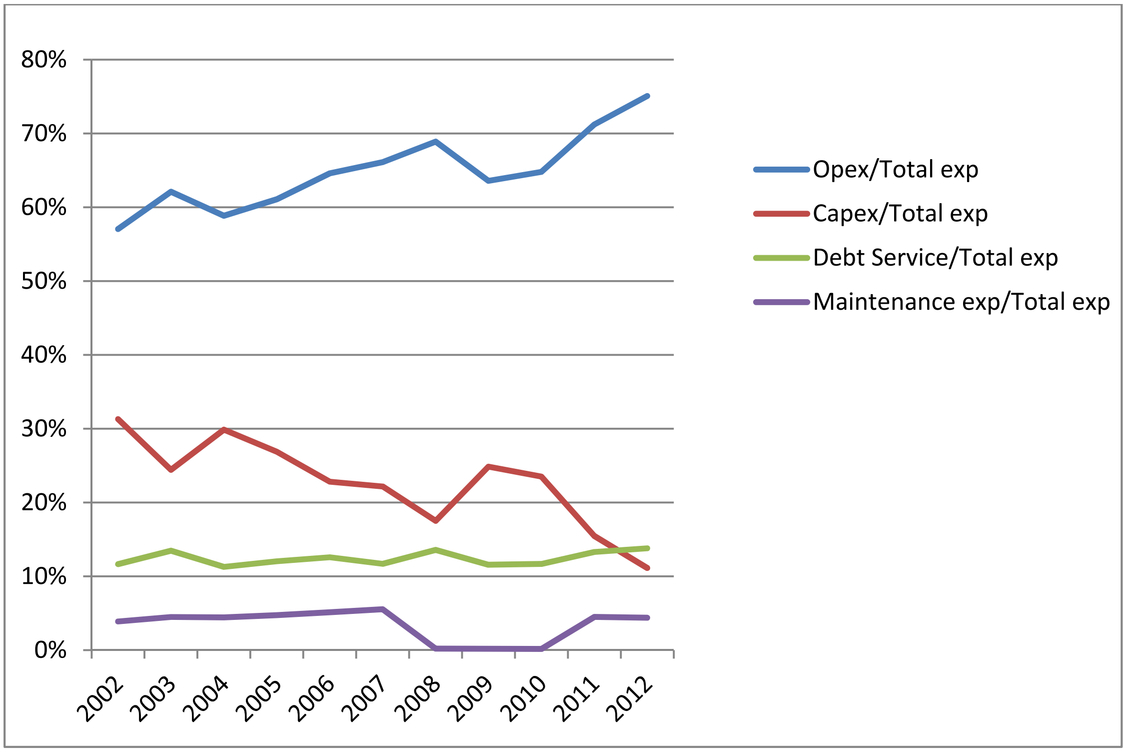
Table 4.3: Capital Grant financing for Municipal investments: 2002-2012

	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012
PIC	42.1	30.4	85.2	56.1	36.1	31.7	31.2	64.6	109.8	31.8	25.0
Hors-PIC	21.4	9.1	9.1	5.2	6.6	3.7	11.2	13.3	25.3	13.5	7.5
PNRQP	6.2	7.2	20.5	25.4	11.2	12.3	13.7	35.1	39.6	10.3	13.9
Others	0.0	0.0	0.0	0.7	2.0	1.7	0.4	0.5	12.3	2.3	3.5
Total	69.7	46.7	114.8	87.3	56.0	49.4	56.5	113.5	187.0	57.8	49.8

Source : Municipal Finance Report, Sinet 2013

27. **Municipal budgets and levels of investment in municipal infrastructure are modest** for a country with Tunisia's degree of economic activity and stage of urbanization. Over the period of 2002 to 2012, LG budgets have remained small despite the extent to which the country is urbanized. Aggregate municipal budgets are estimated at around TND 814 million in 2012, accounting for 1.2 percent of GDP and 3.6 percent of national revenues. Municipal revenues have grown at an annual rate of 6.4 percent over the 2002-2012 period. Adjusted for inflation and population growth, this translates into modest growth in municipal revenues of one percent per capita per year in real terms. Similarly, capital expenditures as well as expenditures for Operations & Maintenance have shown a declining trend while operating expenditures (mainly for meeting staff costs) have been showing an increasing trend (see Chart 4.1 below).

Chart 4.1: Capital expenditures and expenditures for Operations & Maintenance



Source: Bank Team

28. Utilization of the loan facility, notwithstanding the maximum grant per investment provision, has remained constant and about twelve percent less than projected. Similarly, own source revenues have remained relatively constant and about 30 percent lower than projected. The proposed capital grant component of the PIC for 2014 to 2019 of TDN 305 million is equivalent to approximately US$200 million, or about US$5.7 per capita per annum, which represents a slight increase in real terms at rates similar to previous cycles after accounting for inflation and population growth. The grants were fully utilized in both PIC periods. When own source revenues and loans are included, the average annual per capita expenditure for the past two PIC cycles, taking into account population growth and inflation, is roughly equal, at about US$12, as compared to the projected expenditures for 2014-2019 of US$16 per capita per annum, which anticipates significant increases in own source revenues and loans, an assumption that does not reflect past expenditure patterns.

29. The Program is bringing a critical shift in the financing and expenditure model for capital grants. Currently the municipalities are forced to adopt a financing mix comprising of capital grants (PIC allocations), loans provided by CPSCL and a pre-specified share of own revenue contribution. As a result, municipalities are able to access grant funds only after they have availed themselves of loans which have resulted in many municipalities having taken on debt when they did not require such loans or could not afford them. An adverse consequence of this model has been that municipalities with weak revenue and tax base and often with significant demands for urban services are not able to access grant funds as they are already severely indebted. The Program aims to reform this model by delinking the capital grants from loans and in this regard the Government has already issued a Decree and Circular that clearly delinks capital grant allocation from debt financing. Accordingly, allocation and disbursement of capital grants will be made of a simple set of criteria that incentivizes municipal performance rather than their ability to borrow. In addition, a significant aspect of the reform of the capital grant system will be the replacement of the existing system of ex-ante review and clearance of project proposals with an ex-poste review of Program implementation and results which will be elaborated in the Program Operations

Manual. This is expected to expedite the approval, allocation and disbursement of the capital grants annually.

30. As part of the annual allocation process for Capital Grants, municipalities will be required to satisfy certain Minimum Mandatory Conditions (MMCs) upon which they will be allotted their eligible annual capital grant allocations. The annual allocation of the unconditional capital grants (horizontal) will be based on a formula that will be communicated to the municipalities well in advance. The allocation for the Conditional Capital Grants will be based on the municipalities satisfying the MMCs specific to the conditional grants in addition to the MMCs for the unconditional grants. Those municipalities that satisfy the MMCs will receive their eligible grant allocations from CPSCL at the start of the financial year. The CPSCL transfers the necessary funds to the account at the Postal Service (CCP) maintained by the accountant of the Local Government (*receveur*), who will in turn make payments based on payment invoices issued by the municipality.

4.2 Expenditure Framework Assessment

31. The expenditure framework assessment has revealed that the MoEF makes adequate budget allocations every year as a matter of course for meeting the financing requirements of the annual plans. However, in the current system, municipalities do not receive any advance information on the annual allocations nor do they know the list of specific projects that will be allotted funding. This makes municipal budgeting a guessing game and results in inefficient and unaccountable allocation of budgetary resources. The Program aims to reform this model introducing a process whereby MoEF provides information on indicative capital grant allocations in advance to municipalities and in turn municipalities are better able to prepare their annual investment plans and budget in a more realistic manner. Under the previous system, allocation of capital grants based on a project basis following a series of ex-ante review and control processes had resulted in significant delays in project implementation and the consequent delay in the utilization of budget allocations which led to the accumulation of budget allocations in the hands of the implementing entities. Recognizing this, the MoEF has relaxed its annual fiscal year rule for transfers to municipalities and municipalities are not required to return unspent budget allocations (relating to capital grants) at the close of the fiscal year. With the reform of the capital grant process, this issue is expected to be resolved with a more efficient financial planning and budget execution system in place.

32. Another related issue regarding the Program Expenditure Framework relates to the difficulty in obtaining a clear picture of the various fiscal and financial flows to LGs from the existing budget documentation for a variety of reasons. First, the specific booklet for the CPSCL is not public and is with the Government's representative at CPSCL (*administrateur*). Second, a number of financing flows are directly on the budget of line ministries and it is not clear whether they are for operating or investment expenses and whether there are certain conditions attached to their use. Besides, they are not processed through the CPSCL but directly within the Treasury Single Account system and are not consolidated in terms of reporting. To address this issue and to bring about greater transparency in local governance, the DGCPL is designing an E-Portal that will provide comprehensive data on the spatial, demographic, financial, and service delivery aspects of municipalities.

33. The sustainability of the investments being made by municipalities through the capital grants will depend on the ability of the municipalities to improve the mobilization of their own revenues as well as on the ability of both Government and the municipalities to restructure the municipal lending program. Municipalities face an increasingly serious problem of growing municipal debt, driven largely by the requirement that they borrow from the CPSCL to finance their capital investment program according to the ratios described above. Consequently, although the LGs appear to have relatively stable net operating surpluses at around nine percent of recurrent revenues, the extent of the problem is hidden by repeated

rescheduling of the debt under the direction of the MoEF and by supplements provided through exceptional transfers to cover increasing recurrent costs, including debt obligations to CPSCL for infrastructure investment loans (the exceptional transfers are now regularized through the newly created *Fond de Cooperation* – FDC). Current LG arrears on CPSCL loans are illustrative. Over 120 LGs are in arrears of 90 days or more, and of these 80 LGs owe amounts in excess of TDN 250,000. Over 30 LGs are considered chronically indebted and unable to retire their debts. In addition to the financial implications of the debt, the response to dealing with it includes: relaxing the loan to grant ratios; introducing new operating grant transfer instruments; and providing exceptional transfers. In addition, those LGs capable of raising larger amounts of own source revenues and of servicing larger loans have increasingly commanded a larger share of grant allocations on a per capita basis. All of these responses blur the clarity of the grant system and open it up to increasingly ad hoc functional arrangements.

34. Discussions with the MoEF and the Ministry of Interior have revealed that the Government of Tunisia is conscious of the serious debt overhang over municipalities and are desirous of reforming the municipal lending system to make it more sustainable. Currently, *Agence Francaise de Developpment* (AFD) is conducting a study to advise the CPSCL on how to redesign their lending policies and appraisal methods with the objective of transforming CPSCL into a financial intermediary that will operate in accordance with the rules and regulations applicable to financial institutions. Though there is an ongoing program for debt rescheduling for the seriously indebted municipalities, the Program will work with DGCPL to put in place a financial recovery plan to enable municipalities to undertake prudent debt management strategies and will provide necessary incentives for their speedy implementation including incorporating them into the Performance Assessments. Also, the Program will incentivize municipalities to improve own source revenue mobilization by including this as a key performance area under the performance measurement system. In addition, efforts are underway to carry out a PEFA assessment of LGs that is expected to enhance the Public Financial Management framework of municipalities.

35. The Program will be included in the annual budget of the Government under the budget allocation head for the Ministry of Interior. Indicative allocations for capital grants will be included in the five-year plans and the LGs will be informed by July 1, in advance of the preparation of their annual investment plans and budgets. The annual capital grant allocations will be included in the annual investment budget of the Government and will appear in the Ministry of Interior's budget as transfers through the CPSCL[29] (Titre II, line 2.1[30]) to the LGs. The annual allocation for the conditional and unconditional grants, as well as the funds for the capacity building requirements will be included in the national budget under the existing budget line in the name of the CPSCL, and will include a brief description of the allocations for each of the elements of the Program. The Program Operations Manual will describe the operating rules for the budget allocations for the various elements of the Program. The budget allocations for Program elements will be transferred from the Treasury Current Account of the MoEF to CPSCL, which will act as the Program Manager for the capital grant program. CPSCL will in turn transfer the grant funds to LGs as well as other Program implementing entities in accordance with the Decree and Program operating rules. The budget allocations for the conditional grants will be made by the MoEF based on the requisition submitted by the CPSCL.

V. Description and Assessment of Program Results Framework and M&E

[29] *Caisse des Prêts et de Soutien des Collectivités Locales* (CPSCL), is a municipal development fund operating within the jurisdiction of the Ministry of Interior (MoI), but reporting to its own Board. CPSCL was formed by Article 4 of Law No 75-37 of May 14, 1975, and operates under the provisions of Decree 97-1135 as issued in 1992 and amended in 1997.

[30] See link http://www.finances.gov.tn/index.php?option=com_jdownloads&Itemid=712&view=finish&cid=537&catid=1&lang=fr p. 15 of the document

36. The Program will be monitored and evaluated through the use of a number of M&E tools throughout implementation, including regular reports from the LGs to the CPSCL, the Annual Performance Assessments (initially, for the first three years the annual statements of conformity with the MMCs as audited by the Controller General of Public Services) and the Midterm Review.

37. Under current systems, CPSCL has maintained up-to-date, real time monitoring of physical works in all LGs. Under the Program, an E-Portal is being established to monitor LG operations across a number of parameters, and CPSCL will now feed this data into the E-Portal once it has become operational (end of year 1 of the Program). To-date, reliable basic financial information on revenues and expenditures of LGs has been uneven. Under the Program, the MMCs proscribe timely preparation of final accounts for all LGs, and the CPSCL will also upload this revenue and expenditure information from the final accounts into the E-Portal from the end of the first year.

38. The primary source of essential information, and the major M&E tools to verify the performance of the LGs are the annual MMCs and the results of the PAs (which will also be entered into the E-Portal). The PA will be carried out in line with the PA manual, which will be finalized and adopted by the end of 2015, with its content and quality acceptable to the Bank. The manual will provide clear definitions for each indicator, as well as comprehensive guidance on the scoring. Adjustments, which mightneed to be made to the performance indicators and scoring, will be done during a dry run of the system in 2016. Future adjustments will be made as needed in light of the experience and all these sources will be captured by CPSCL in preparing its annual Program progress report. The data from the assessments will be uploaded onto the E-Portal, together with the revenue and expenditure and physical works progress, and will be used both for preparing annual consolidated reports by CPSCL, as well as for tracking progress against projected results.

39. Progress towards the Program Development Objective will be measured through a set of measurable indicators, utilizing the data on the E-Portal; most of them will be linked to disbursements. The Results Framework for the Program has three key results areas that are closely inter-related. Each results area is linked to DLIs, Program Actions and planned capacity support, as well as to monitoring, evaluation, and verification activities in the Program. This provides a coordinated incentive for LGs to improve their institutional capacity to perform their essential functions. The Results Framework is provided in Annex 2, while the detailed table of DLIs is provided in Annex 3. These results and their associated results chains are:

39. **Result Area 1: Capital Grant System Reformed:** The targeted outcomes of the Program in this Intermediate Results area are: (a) the LGs are given timely confirmation of their indicative capital grant allocation for the forthcoming year (July 1) so that they can utilize it effectively in preparing their municipal investment plans and their capital budgets, and the funds are transferred in a timely manner to their accounts for application to the funding of their budgeted investments (March 1); and (b) that the eligible LGs meet the required MMCs in order to qualify for disbursement of their grant entitlement. The targeted outcomes in this result area are addressed by DLI 1 and 2, which stipulates that the Reformed Capital Grant system is fully operational, and measures this through a series of annual requirements, starting with the adoption of the amended Decree in the first year, and then stipulating dates for confirmation of each LG's indicative grant allocation (July 1) and for the release of funds to the LGs (March 1). The adoption of the Decree is pivotal as it comprises a series of clauses that regulate all the elements of reform that the Program seeks to support (the adoption of an objective allocation formula; the timely release of the annual allocations; the provision that determination of the use of grant funds is solely at the discretion for the LG; that the LG should demonstrate effective participatory investment planning; the delinking of the grants from the loans; the phased introduction of the performance assessment system; and the requirement that the assessment be undertaken by an independent agency and that its findings be

made public in a timely manner). DLI 3 addresses the other outcome of this Intermediate Result by stipulating annual targets for the minimum number of LGs satisfying the MMCs.

40. **Results Area 2: LG institutional performance improved to deliver municipal infrastructure and services:** The targeted outcomes in this results area are: (a) the LG performance assessment system established and fully operational; (b) that the LGs are implementing their Annual Investment Plans on schedule; (c) that capacity support to the LGs is provided according to their annual capacity support plans; and (d) that information on the grant transfer that each LG receives and on the results of the LG's Performance Assessment are publicly accessible. The DLIs address these outcomes as follows: DLI 4 sets out annual benchmarks to be achieved for phasing in and making operational the performance assessment system; DLI 4 stipulates also the percentage of LGs achieving annually rising minimum levels of expenditures on capital works specified in the LGs' investment plans; DLI 6 takes account of the number of LGs that have implemented their annual capacity development plans; and DLI 8 addresses the access to information outcomes sought under this results area as follows: in CY 2015, it requires that the E-portal be up and running; in CY 15, CY 16 and CY 18 it requires that a target percentage of financial accounts legally received by the Court of Auditors (*Cour des Comptes*) be audited by September 30 each year with the target set at 80 percent for CY 18.

41. **Results Area 3: Access to municipal infrastructure in targeted disadvantaged neighborhoods improved:** The expected outcome under this results area is improved access to municipal infrastructure in disadvantaged neighborhoods within the 144 targeted municipalities. DLI 7 requires that the Investment Plans by the targeted LGs for investment in the selected disadvantaged neighborhoods are executed according to schedule, and provides annual targets to be met measured in percentage of target population for which works have been tendered and for which works have been completed, with works completed for a target population of 500,000 by the final year.

VI. Program Economic Evaluation

42. The following economic analysis contains several analyses. It provides an analysis of the development impact of the Program through economic return, alternative project, risk, and fiscal sustainability analyses of this project. It outlines measures to facilitate continued economic analysis of the project, provides a rationale for public sector provision and financing, and explains World Bank value-added.

Development Impact

43. The expected development impacts of the Program are improvements in: the infrastructure and services provided by LGs in Tunisia for all of their residents; LG capability to deliver infrastructure and services; and the relationship between Tunisians and their Government. Despite gains in access to infrastructure and basic services in Tunisia over the past two decades, large disparities remain in access to basic services administered by LGs (namely public sanitation networks and local roads). Approximately 25 percent of Tunisians are disconnected from a public sanitation network with substantial differences in access within and across LGs.[31] Poor sanitation network connections can lead to higher incidences of illnesses such as diarrhea compromising the health of relevant populations and their financial resources due to the costs associated with these illnesses. In 2004, a study estimated that the annual costs associated with diarrheal incidence in Tunisia were between 11 and 56 million TND.[32] Citizen discontent

[31] For instance, only 7% of homes in Tunis have no connected to public sewerage system while 88% of homes in Sidi Bouzid do not have access to public sanitation service (WB 2013).

with services under the mandate of LGs was indicated in a recent survey conducted by the Bank of Tunisian citizen perceptions of Government provision of services. Poor local road networks are associated with constrained access to markets. The January 2011 Revolution highlighted the grievances of marginalized populations in Tunisia and the large-scale impact that neglecting those grievances can have on development and prosperity across the country; as such, the dual goals of helping marginalized Tunisians attain a minimum standard of quality of life and improving the relationship between citizens and Government are urgent priorities for the Government. More detailed economic analyses of the project are provided below.

Economic rate of return

44. The measurement of economic rates of return (ERRs) for LG strengthening programs is not straightforward for several reasons. Reform of the inter-governmental capital grant system is designed to empower LGs and their citizens, hence the specific investment projects that will be financed through the grant(s) supported through this Program are unknown at this stage. Furthermore, the projects that can be undertaken by LGs with the support of this Program – particularly local roads, drainage network connections, and street lighting – are small-scale with many of the benefits non-rigorously quantifiable. The Government has not mandated economic analyses for these types of projects in the past, hence no data exists that could be used to quantify the benefits of similar projects in Tunisia. Rate of return analysis is even more difficult to do in a rigorous and credible manner for institutional development strengthening activities.

Nevertheless, there is evidence of positive returns for some similar local Government support projects that have been supported by the World Bank in other countries. In Uganda, an assessment of the first Local Government Development Program (LGDP1) found that the ERR of the small infrastructure projects provided through LGs was above twelve percent.[33] A similar project in the Philippines – the Local Government Finance and Development Project – yielded an ERR of 35 percent.[34] Although the context and the exact bundle of investment projects vary, these findings indicate that if well-designed and implemented, this Program could generate positive economic returns.

Productive efficiency

45. The proposed reform of the inter-governmental capital grant transfer system and the institutional development strengthening activities are expected to increase the productive efficiency of LGs. Productive efficiency has been achieved in settings where citizens were better able to hold LGs to account, where fewer tiers of Government were involved in service delivery and the tier providing the services had better knowledge of local costs.[35] World Bank studies have found that in many cases, infrastructure delivered in decentralized contexts was of higher quality and was completed at lower cost than in more centralized settings, and that results-based approaches to municipal development achieved more sustained impacts.[36] For instance, the cost effectiveness of local roads produced in the Uganda LGDP-I project was in the range of 32.6 percent - 38.9 percent of the total investment.[37] Furthermore, the greater scope for decision-making, technical support to enhance learning by doing, and accountability loops introduced through this project are expected to help increase the organizational performance of LGs.

Allocative efficiency

[33] World Bank ICR 2008
[34] World Bank ICR 2009
[35] Kahkonen and Lanyi 2001
[36] Martinez-Vasquez 2011, IEG 2008, and UNCDF 2008.
[37] World Bank ICR 2008

46. Greater discretion[38] over the use of their resources is expected to improve the allocative efficiency of LG infrastructure and service provision. International experience demonstrates that LGs are capable of better allocating resources according to citizen preferences than central Governments when they have adequate discretion over the use of resources and when citizens can monitor LG performance.[39]

Alternative project considerations

47. Several alternatives could have been pursued in place of the proposed Program. One option would be for the Government to continue with business as usual. Under this scenario, the deterioration of the provision of LG services and infrastructure, and the financial health of LGs was likely to continue. Alternatively, the Government could have pursued an emergency project to provide basic infrastructure and services through central authorities rather than through LGs. This measure could have been justified on the grounds of the urgent need to address these basic needs of citizens and alleviate social tensions associated with the 2011 Revolution. However, it would have further undermined LG authority. It also would have foregone a critical opportunity to foster accountability mechanisms between citizens and the Government. Other program design parameters could have been altered, and several such considerations were made during Program preparation, but the proposed design reflects a consensus regarding the design that promoted the greatest development impact given existing constraints.

Future assessments

50. A dearth of data limited the scope of this development impact analysis. More importantly, this dearth of data limits knowledge of the efficacy of a range of development interventions in Tunisia. Support for performance monitoring and other components of M&E to accompany this program are designed to help improve the outcomes of the Government program, and to increase the availability of data to assess the merits of similar development interventions that may be undertaken in the future in Tunisia.

51. Regarding LG investments in specific, the Program will support the introduction of measures to assess the economic impact of Tunisian LG infrastructure investments. As a result of the narrow mandate of Tunisian LGs, infrastructure and basic service provision projects are micro projects, and with the exception of revenue-generating investments (which are outside the scope of this project), have not necessitated project-level economic analyses based on Government investment criteria. As such, despite decades of Bank support for Tunisian municipal development projects, there has never been data to conduct traditional cost-benefit and cost-effectiveness analyses of relevant Tunisian investments. Through the Program, the Bank will assist the Government to introduce economic analyses of LG infrastructure and basic service projects through the feasibility studies that will be conducted for the disadvantaged neighborhood projects.

Rationale for Public Sector Provision and Financing

52. There is a strong rationale for public financing of the activities supported under the Program. Specifically, the rational for public sector provision and financing is that (i) the investments are local public goods; and (ii) no negative substitution effects are anticipated.

[38] Combined with greater citizen participation and enhanced accountability mechanisms.
[39] For example, local budgets better matched citizen priorities after further decentralization in Uganda & the Philippines (Martinez-Vasquez 2011).

53. **Most of the Program investments are in public goods.** The municipal investments eligible for support under the unconditional and conditional grants are at least in part local public goods, and therefore likely to be undersupplied by the market. These include municipal roads, street lighting, drainage, water supply and sanitation, solid waste management, and local social and economic infrastructure. The provision of these goods is under the responsibility of LGs as per the 2014 Constitution, in keeping with commitment to achieve a more efficient and closer administration to citizens.

54. **No negative substitution effects.** The Program focuses on improving the efficiency of transfers for infrastructure investment and capacity of LGs to select and implement projects. It is therefore not expected to lead to any substitution effects on infrastructure investment. The projects will continue to be selected through guidelines for preparation and evaluation of subprojects outlined in the Program Operational Manual, although LGs will be given full responsibility and autonomy for the selection, preparation and execution of local investments supported by the grants. The allocation and implementation of funds is therefore expected to improve with the project, and is not expected to have any new negative substitution effects.

World Bank Value-Added

55. The World Bank adds value to the Program through financing, relevant and operational expertise, and by its ability to help leverage additional resources.

56. The institution has extensive experience supporting Inter Governmental Fiscal Transfer System Reform, programs to strengthen LG capabilities, and programs to increase access to municipal services and infrastructure in Tunisia and around the world. The World Bank has supported consecutive municipal development programs in Tunisia since 1992. More broadly, the World Bank has supported decentralization efforts in more than 89 countries in the world since the 1990s, including in Morocco, Jordan and West Bank and Gaza in the Middle East.[40] An IEG assessment of a subset of World Bank decentralization operations found that the impact of many of these operations was weak in the 1990s but improved considerably in the 2000s.[41] This improvement may be attributable in part to World Bank staff disseminating lessons learned as appropriate to other projects over time. These lessons range from the importance of pairing certain reforms to the necessity of having effective performance monitoring systems in place and in use. Such lessons have been reviewed and have informed the World Bank's engagement with Tunisia on this Program.

57. Furthermore, the World Bank can help relevant parties in the Government leverage support for its LG development program as it undertakes this set of reforms in a politically challenging environment. Reform of the distribution of national wealth, and of formal linkages and practices that change the relationship between different levels of Government and between Government and society are by definition challenging to accomplish. The current socio-political context provides both an impetus and a constraint to the successful introduction and implementation of such reforms. The involvement of a relatively neutral actor – the World Bank – in helping facilitate the national dialogue and deliberations needed to define and introduce these reforms can help accelerate and improve the outcomes of these efforts. Furthermore, the Bank's commitment to this reform program has helped attract additional development partners to support certain dimensions of the reform program.

Inputs to the Program Action Plan

[40] IEG 2007
[41] IEG 2008

Table 4.5: Program Action Plan

Area 1 – Transparent capital grant system
1. Decree 97-1135 replaced to introduce transparent formula based allocation of capital grant for municipal infrastructure delivery
2. Ministerial Decree published indicating the annual allocation of capital grant for municipal infrastructure delivery
Area 2 – Municipal performance assessment
3. Preparation and approval of the LG Performance Assessment Manual
4. E-portal designed and implemented
Area 3 – Municipal capacity building
5. Annual Capacity Development Plans prepared by all LGs
6. Preparation of standard terms of reference for feasibility studies of investments in disadvantaged neighborhoods
7. ESM developed that provides updated procedures for environmental and social management for LGs to address gaps identified in the ESSA, including: (i) public consultations, public disclosure and grievance redress mechanisms; (ii) social assessment; (iii) land acquisition and resettlement procedures; (iv) screening of high-risk activities which are ineligible for Program support; and (v) monitoring and evaluation.
8. Specific training modules consistent with the provisions of the POM have been developed and are made available to the LGs
9. Specific training modules on financial management for municipal financial management staff are developed and a national wide training program is initiated
Area 4 - Country systems improvement
10. A revised decree is adopted by the ANPE which addresses gaps identified in the ESSA, including (i) screening and categorization of activities requiring an EIA or an EMP; (ii) public consultations, public disclosure and grievance mechanisms; (iii) social assessment; and (iv) monitoring and evaluation.
11. The capacity of the *Cour des comptes* and in particular its local branches is improved in order to perform annual financial audits of municipalities based on risk and in compliance with international norms of auditing (ISSAI).
12. Municipalities to prepare and implement annual action plans to address audit findings within a period of six months after the receipt of the audit report
13. Citizens Bureau in each municipality to be operationalized and their performance in grievance resolution monitored by the municipal councils
14. Good Governance Cells established in all municipalities by the second year of the Program

Technical risk rating

58. Although CPSCL, in charge of day-to-day management of the Program, has significant experience implementing similar Municipal Investment Program with World Bank support, and has operated in concert with all the LGs to be supported under the Program, the overall risk rating is substantial due to country circumstances, the fiduciary implications of shifting form an ex ante to an ex

post system of oversight; and the emphasis on improved performance by the 264 LG stakeholders for undertaking functions that currently represent their weakest areas of capability. The shift from a *tutelle* system to one of decentralized authority and accountability is transformational, and represents a substantial level of risk in a country undergoing a transition..

Annex 5: Fiduciary Systems Assessment Summary

Introduction

1. As part of the preparation of the PforR Program, the World Bank task team carried out a Fiduciary Systems Assessment (FSA) of the Program in accordance with OP/BP 9.0 of the World Bank Operations Manual. The objective of the Assessment was to examine whether Program systems provide reasonable assurance that the financing proceeds will be used for their intended purposes, with due attention to the principles of economy, efficiency, effectiveness, transparency, and accountability. Accordingly, the Program procurement assessments were assessed to find out the extent to which the planning, bidding, evaluation, contract award and contract administration arrangements and practices provide a reasonable assurance that the Program procurement systems will enable the achievement of intended results.

2. The FSA was carried out by an experienced team of World Bank staff that included Financial Management and Procurement Specialists. The team went through the existing country and sector reports, discussed with client counterparts both at the Central Government as well as at the LG levels. The team also visited a sample of municipalities to assess the working of systems on the ground. The initial findings were discussed informally with client counterparts to get validation on the findings and conclusions.

Program Financing and Expenditure Framework:

3. The proposed PforR Program involves an outlay of US$300 million as World Bank financing, and which is part of the overall Government program of financing municipal service delivery. The Government's existing program for financing municipal service delivery includes a combination of capital financing (through PIC allocations), loans to municipalities (through CPSCL) as well as the Own Source Revenues (OSRs) of the municipalities. The proposed PforR operation takes a subset of the Government's program and supports it, the details of which are provided in the detailed Program description section of this document.

4. The proposed Program will be included in the annual budget of the Government of Tunisia under an existing budget line for capital financing of municipalities. The purpose of this budget line will be specified in the budget documents which will describe the allocation of the Program funds for the unconditional and conditional grants under the Program as well as for the capacity building component. Indicative allocations for Capital Grants will be informed to the municipalities in advance of the preparation of the annual plans and budgets. The annual Capital Grant allocations will be included in the annual Investment Budget of the Government and will appear in the Ministry of Interior's budget as transfers to the CPSCL[42] (Titre II, line 2.1[43]). As part of the reform to the existing system of capital grant allocations, the MoEF will issue separate *arrêté* (Government order) that will define the access conditions, as well as operating rules for the Capital grants. The budget allocations for Program elements will be transferred to a designated account at the Central Bank and then to the Treasury Current Account

[42] *Caisse des Prêts et de Soutien des Collectivités Locales* (CPSCL), is a municipal development fund operating within the jurisdiction of the Ministry of Interior (MoI), but reporting to its own Board. CPSCL was formed by Article 4 of Law No 75-37 of May 14, 1975, and operates under the provisions of Decree 97-1135 as issued in 1992 and amended in 1997.

[43] See link http://www.finances.gov.tn/index.php?option=com_jdownloads&Itemid=712&view=finish&cid=537&catid=1&lang=fr p. 15 of the document

of the state at the Central Bank (BCT) from which the Program will be executed. The unconditional capital grants will be disbursed by Treasury to the CPSCL in one tranche by February 1 of every year. CPSCL will in turn transfer the unconditional capital grant funds to municipalities at the latest by March 1 of every year. The budget allocations for the conditional grants will be disbursed by Treasury based on specific requisitions by the CPSCL. The funds for the capacity building component will also be transferred to the CPSCL based on the actual implementation of the capacity building program.

Program Financial Management framework:

5. Financial Management of the Program is proposed to be carried out using Tunisia's existing systems and processes for Public Financial Management. The Program will be located within the country's budgetary framework and will rely on existing institutional systems for implementation. The three entities that will be involved in the financial management and oversight for the Program are:

- *The Ministry of Economy and Finance*: The MoEF is responsible for the formulation of the Budget and its implementation and in particular in relation to the grants transferred to municipalities and other LGs. In terms of Budget formulation, the Budget Preparation Committee (*Comité de Préparation du Budget*) is the relevant entity which coordinates with the various sectors, including the Ministry in charge of LGs (Interior). The General Directorate of Local Finances (*Direction Générale des Finances Locales*) is the General Directorate under the General Directorate of accounting and Resource collection that is in charge of managing the implementation of LGs's budget and transfers to LGS from central Government. This Directorate supervises and manages the network of Government accountants assigned to municipalities (*receveurs*). The Public Sector Accounting Code (*Code de la Comptabilité Publique*) applies at both central and local levels for budget implementation and accounting rules.

- *The Ministry of Interior (MOI)*: The Ministry in charge of LGs is the Ministry of Interior, and in particular the General Directorate for Local Government (*Direction Générale des collectivités Publiques Locales, DGCPL)*. The DGCPL has a monitoring and supervision role ("*tutelle*"), as well as a policy and advisory role towards LGs. The MOI is the "*tutelle"* of Governors.

- The *Caisse de Prêt et de soutien aux collectivités locales* (*CPSCL*): CPSCL was created by law #75-37 of May 14th 1975. It is a non-administrative autonomous agency (*établissement public non-administratif*) now organized according to decree 92-688 of April 16th 1992. It is not a bank and its missions are defined by the Government and aim at economic and social development of municipalities. CPSCL has substantial experience in implementing Bank-funded project and ensuring fiduciary responsibility. Its systems of financial management have been assessed regularly and recently (2013) and have been deemed to provide sufficient guarantee to manage Bank proceeds. CPSCL's FM staff capacity has been assessed and is deemed acceptable. CPSCL also has capacity to monitor the activity of municipalities and to provide advice. CPSCL financial statements are audited annually as per the law by an independent audit firm. CPSCL financial statements are compiled according to business accounting standards.

6. *Planning and Budgeting*: Municipalities' investment budget (*Titre II*) is funded i) through grants that appear in the Interior Ministry's budget as transfers to the *CPSCL (*the *Caisse)* (Titre II, line 2.1[44]); ii) through local tax and non-tax revenues and the balance of previous year's current budget (*auto-financement*). In the existing system, the municipality prepares a financing request to CPSCL based on

[44] See link
http://www.finances.gov.tn/index.php?option=com_jdownloads&Itemid=712&view=finish&cid=537&catid=1&lang=fr p. 15 of the document

the five-year investment plan (PIC). A Financing Committee comprising of representatives from the Ministries of Finance, Interior, Development and Planning as well as the CPSCL approves the request which triggers the procurement process. The whole process takes approximately eight months and everything goes well but municipalities have reported delays and cancelations often due to excessive formality of procedures. According to a schedule of payments, CPSCL transfers the necessary funds to the account at the Postal Service (CCP) maintained by the accountant of the local Government (*receveur*) who makes the final payment.

7. The Program will substantially modify the role of CPSCL as the funds that are provided as capital grants are in the nature of fiscal transfers (unconditional and conditional) instead of project financing. The municipality has the discretion to use the funds to finance capital investment projects of its choice and as reflected in its annual plan and budget. Accordingly, once the municipality satisfies the Mandatory Minimum conditions (MMCs) for gaining access to the funds, CPSCL will disburse the funds to the municipality. Each municipality will enter into a Memorandum of Understanding with the Government through the CPSCL that will spell out the roles and responsibilities for both. The Program Operations Manual will provide details of the frequency and timing of the disbursement of grant funds by CPSCL to the municipalities.

8. *Flow of Funds*: All payments of the Program will be made through the centralized Treasury system of Bank accounts held at the Central Bank of Tunisia (which also uses the network Postal Current Accounts, *comptes chèques postaux, CCP*). For each municipality, the *receveur* is in charge of making the payment and the Tunisian Public Financial Management system, including at the local level, is based on the principle of the separation between those who order payments (*ordonnateurs*) and those who make the payments and record it in the accounting system (*comptables,* here *receveurs*). Program funds will be entirely reflected in the central Government budget under the Ministry of Interior's budget and will then be channeled to municipalities through the CPSCL. For unconditional grants, the funds will be disbursed based on the attainment of minimum mandatory conditions (MMCs) as well as based on a performance assessment later in the Program. These funds may then be mixed with loans and own source revenues by the municipality. For capacity building, the funds will be part of the budget of the MOI and will follow the usual expenditure cycle for the implementation of the Budget.

9. Accounting and Financial Reporting: Accounting principles to be followed by LGs are specified in organic local Budget law (75-35 completed by 2007-65 of 18 December 2007) which details the chart of accounts for the formulation of the Budget as well as for accounting. This is a cash-based single entry accounting. The Budget is voted by the LG's council and after this submitted to the "*tutelle*" for approval. The Budget is annual and comprehensive (all financial operations must be reflected). If a budget is not voted before the start of the fiscal year the expenditures are incurred based on a quota of one twelfth of previous year's budget. Virements and transfers during the year from one credit line to the other are strictly defined by the law. Budget must be balanced between resources and expenditures.

10. The Central Government systems provide strong support to municipal financial management:
(i) each municipality has a Government accountant attached to it (*le receveur*). This accountant is paid and managed by the General Directorate of Accounting of the MEF and implements the Accounting Code which applies to all accountants at central and local levels. This accountant uses the IT systems of the Government (ADEB for expenditures, RAFIC for revenue, SIADE for debt) which are accessible at every point in the system and allows immediate issuance of financial reports. ADEB allows for the production of real-time fiscal situation of municipalities; (ii) this accountant is submitted to a comprehensive control and audit framework (ref. infra); and (iii) the accountant works also with the head of the municipality and municipal staff in terms of resource collection and expenditure cycle. Though generally well structured, this system presents several weaknesses. In particular, the accounting and financial reporting framework

is based on a budget execution framework and the system does not allow for the production of financial statements that would present financial assets and liability. This single entry accounting is also a weakness that is well known and analyzed at the central level where there is an effort to generalize double entry accounting in 2014 and then a plan designed to progressively move towards integration of elements of accrual accounting.

11. Financial information at the LG level will therefore rely on the "*compte de gestion*" produced by the accountant and sent systematically to the Cour des comptes. These end-of-year accounts provide the annual balance of all accounts used by the LG for collecting resources and incurring expenditures. The capacity of these *receveurs* has been evaluated and is satisfactory. They are part of a national cadre of Government accountants and are recruited through competitive exams. They are on average well trained and skilled.

12. *Controls*: The control framework comprises several layers. They are:

- Controls by the CPSCL: CPSCL follows a good set of internal control procedures before making disbursements to municipalities. The funds are released through a check which cannot be used for other purposes than the payment it is meant to cover (*fonds affectés*). The accounting department of CPSCL also follows separately payment arrears of municipalities, for which central Government is the guarantor. ADEB, the IT system used by Government accountants (including at the municipal level) is accessible at CPSCL. The Internal Audit Unit of CPSCL is well staffed and includes the Program within the scope of its work and will submit reports to the Board of Directors of CPSCL.

- Controls by the Central Government: The expenditure cycle for municipalities is submitted to the same controls than for central Government expenses. The General Controller of Expenses (*Contrôle Général des Dépenses*) under the Prime Minister's office has to approve ex ante, at the commitment stage, every single expense through the ADEB system. Then the *receveur* has to control the whole process and the justifications before making the payment (*contrôle concomitant*). This systematic ex-ante control is being reformed at the central Government level and is evolving towards a more strategic and risk-based approach. This system of ex-ante control of expenditures should be progressively extended to the control of municipalities' expenditures, which would be in line with the objectives of the Program as well as with the formulation of the new Constitution. The General Inspectorate of Interior implements an annual program of controls that involves a substantial sample of municipalities each year.

13. *Audit of Local Governments*: The Court of Auditors (*Cour des comptes*) has been the external auditor of LGs for a long time and it is equipped with a dedicated chamber at the central level (seven magistrates) as well as four regional chambers covering the entire territory. Currently, the Court of Auditors (*Cour des comptes*) audits all LGs for all fiscal years but with an average regularity of between three to five years. These audits are meant to be compliant with INTOSAI norms and vary in intensity and modalities based on the size and risk level of the municipality. Some municipalities are audited based on a desk review and a questionnaire. Others receive regular visits of auditors. The Court of Auditors (*Cour des comptes*) also conducts performance audits of municipalities, either on a regional basis or on a thematic basis or both.

14. For the Program, the Court of Auditors (*Cour des comptes*) would need to audit annually all municipalities, which represents a substantial performance increase from the current practice. Nevertheless, the President of the Court of Auditors (*Cour des comptes*) has agreed with the Bank in principle to increase annual coverage of annual external audit of municipalities and schedule them progressively. It has also been agreed that capacity building support will be provided to the Court of

Auditors (*Cour des comptes*) under the Program that will enable it to carry out the annual external audit of municipalities in a timely manner.

15. *Disbursement arrangements from the Bank*: Disbursements of the IDA credit proceeds will be made at the request of the borrower upon achievement of Disbursement-Linked Indicators (DLIs). Loan proceeds will be disbursed into a designated account at the Central Bank and then to the single treasury account of the state held at the Central Bank. Disbursement requests will be submitted to the Bank using the Bank's standard disbursement forms thru the e-disbursement functionality in the Bank's Client Connection system. It was identified that advances under the PforR operation might be necessary in order to allow the borrower to achieve the results for one or several DLIs. Accordingly, at the start of the Program, the Bank will provide 20 percent of the total credit as advance and 10 percent for the attainment of the prior result agreed to.

16. *Program Financial Management Risk Assessment*: The lack of a comprehensive information system at the municipality level and at the aggregated level is a major weakness that emerged during the preparation of the Program and that has been noticed by the Court of Auditors (*Cour des comptes*) in its various audits. The creation of an e-Portal, which has been envisaged as part of the Program could efficiently mitigate this risk if it is accompanied with a substantial effort to design a system of data collection for municipalities.

17. The CPSCL and municipalities have substantial cash reserves amounting to respectively (200 MTND and 350 MTND), which has been confirmed by the Director General of CPSCL. To mitigate the risk of funds getting accumulated at the municipal level without being spent, the Program has built in mitigation measures such as monitoring and rewarding municipal performance, initiating a regular and timely system of external audits, strengthened social accountability processes such community participation, and sharing of information through the e-portal.

18. The controls and audit framework related to LGs provides some level of fiduciary comfort but at the same time, these controls are redundant, overlapping and seem to create risk avoidance behaviors if not situations of failure to implement projects. The Program will help promote a new balance through a strengthening of ex-post controls and audits and less stringent ex-ante controls on expenditures. The Program is also putting in place a robust capacity building program for financial management that will provide traditional classroom training as well as just-in-time capacity support through mobile technical teams.

19. Nevertheless, the PFM systems in the country are generally considered good by international standards as it is reflected in the 2010 Tunisia PEFA assessment. In particular, PI-8 on inter-governmental fiscal relations has received a score of B. It is assessed that Program's Financial Management arrangements relying on country wide system are acceptable in terms of procedures and results after appropriate mitigation. The country-wide system helps central Government and LGs (i) to keep close control of fiscal risks and to maintaining overall budget discipline; (ii) to plan and execute the budget in line with its set priorities; and (iii) to effectively manage public resources to deliver services. The country PFM at central and local levels gives reasonable assurance that fiduciary risks would be maintained at substantial level and could be mitigated through the implementation of appropriate mitigation measures; the Program can be implemented through the existing PFM system, provided that some identified challenges, at the country and local levels, are addressed, either through the PAP or other initiatives (accounting and reporting, internal and external audit). Based on the elements above, the overall fiduciary risk is rated Substantial.

Program Procurement Systems

20. Though historically the public procurement system was bureaucratic and unnecessarily procedural, lacking transparency and accountability, there has been a significant change in the system after the Revolution. The Interim Governments have embarked on the revision of the existing public procurement decree to address the major weaknesses while ensuring transparency and efficiency of the system. In parallel, the Government launched with the World Bank and African Development Bank's support a thorough review of the procurement system using the (OECD-DAC/MAPS) Methodology for the assessment of procurement systems to undertake a more comprehensive reform in order to modernize the institutional and regulatory frameworks in line with international standards. This exhaustive review has resulted in the enactment of a consolidated and revamped procurement decree (No 2014-1039 dated March 13th, 2014) which has come into effect on June 1st, 2014. This decree which applies to all local Government levels when they act as public procuring entities has filled in several gaps with international good practices as mentioned in the action plan annexed to the MAPS /OECD-DAC self-assessment report dated August 2012.

21. *Municipal Procurement procedures:* Municipalities are responsible for the entire procurement process and contracting process, which encompass the following: (i) planning; (ii) preparation of bidding documents; (iii) receipt and evaluation of bids or proposals; (iv) finalization and signing of the contract; (v) monitoring the execution; and (vi) filing and archiving documents. Large municipalities have an officer (*Receveur Municipal/Tresorier)* at the level of the Municipality and small municipalities have one at a higher level (*Recette des Finances*). However, each governorate has a Regional Office (*Bureau Regional de Controleurs de Depenses)* in charge of conducting ex ante control of procurement processes within the Municipal or Regional procurement committee. This office (*Bureau Regional de Contrôleurs de Dépenses*) is in charge of all procurement oversight at the regional (governorate) level which includes, inter alia, municipality's procurement.

22. *Technical preparation, technical oversight and technical Audit*: Municipalities manage core procurement processes (such as preparation of bid documents, design of construction and infrastructure works) in a variety of ways. While large municipalities have their own strong in-house capacity, small and medium municipalities rely on technical support from the deconcentrated line ministries at the Governorate level or contract out with private sector consultants. For the PforR Program, the Ministry of Interior may keep a technical oversight role, but it is mainly the role of CPSCL to provide technical oversight including physical field inspections. The procurement processes at the municipal level are subject to various levels of oversight and approvals. Based on the cost estimate for a contract, the municipality would be subject to one or more of the following procurement committees each of who have their specific thresholds for approval. Before going to the High Tender Board, all steps of procurement subject to prior review shall be submitted first to the ministerial procurement committee for a preliminary prior review before being submitted to the High Tender Board:

	Local/Municipal committee	**Regional Committee**	**Ministerial Committee**	**High tender Board**
Works	Up to TND 2 millions	Up to TND 5 millions And up to TND10 Million for regional projects	up to TND10 Million	above TND10 Million
Goods and non-consulting services	Up to TND 400K	Up to TND1 million	Up to TND 4 million	Above TND4 million

IT equipment	Up to TND300 K	Up to TND1 million	Up to TND4 million[i]	Above TND4 million
Software and IT services	Up to TND300 K	Up to TND500K	Up to TND2 million	Above TND2 million
Consulting Services (Etudes)	Up to TND150 K	Up to TND200 K	Up to TND300 K	Above TND 300 K
Preliminary breakdown of estimated quantiti and cost	Up to TND2 Million	Up to TND5 Million	Up to TND7 Million	Above TND7 million

23. All commitments are submitted, before contract signature, to the prior clearance by the *Controleurs de Depenses* (as per art. 12 of Decree no2012-2878 dated November 19th, 2012 governing the *Controle des Depenses Publiques*. Only Municipalities whose annual budget exceeds and amount to be defined by decree have their own municipal procurement committee except the Municipality of Tunis which has its own procurement committee whose competency thresholds are up to those of the High tender Board. The new decree provides for various procurement methods such as Quality and Cost Based Selection, QBS: Quality Based Selection and LCS: Least Cost Selection.

24. The procurement methods thresholds are summarized in the table below:

	Purchase Order	Shopping (simplified procedures)	Competitive bidding
Works	Up to TND200 K	Up to TND500 K	Above TND500 K
IT Goods and services	Up to TND100 K	Up to TND200 K	Above TND200 K
Other Goods and services	Up to TND100 K	Up to TND300 K	Above TND300 K
Consulting services	Up to TND50 K	Up to TND100 K	QCBS, QBS and LCS[ii]

25. The new decree has also brought about the following changes in the procurement procedures: (i) simultaneous opening of technical and financial bid envelopes in the same public session; (ii) publication of invitations to bid, awards, and decisions of the complaints body in the web based public procurement portal; (iii) introduction of a standstill period for complaints, (iv) higher prior review thresholds, (v) post reviews for small contracts; (vi) reduction of the award process mandatory minimum duration. It must be noted that the threshold for entities' own tender committees or *Commission d'achats* allows municipalities to procure or purchase without seeking review and clearance of the Governorate level regional tender boards – the *Commissions regionales des marches*- has been raised up to the new shopping threshold of 500K TND for works, 300K TND for goods, 100K TND for consultancy services (approx. 50K Euros).

26. There are several aspects of the institutional systems for public procurement that can be helpful to the Program. An electronic procurement System called "*Tuneps*" is being piloted which could possibly be scaled up to municipalities. The national public portal of the *Observatoire des Marches publics* – National Observatory – is operational and available to all national procuring public entities including municipalities for mandatory advertising of procurement opportunities and for the upcoming publishing of awards rendered mandatory under the new procurement decree.

27. There is a functional system for handling complaints relating to public procurement and municipalities come within their ambit. The Market Monitoring Committee (*Comité de Suivi et d'Enquête*

sur les marchés publics, COSEM) is part of the HICOP and is responsible for receipt, follow up and resolution of procurement complaints. According to the new procurement decree, COSEM decisions are now binding and no longer consultative, and a new standstill period of five days is slightly increased compared to three days previously, however it remains less than the international good practice of ten days. They also are periodically advertised on the public procurement portal, and therefore access to information is furnished to all citizens.

28. However, there are a few weaknesses in the system that could potentially result in a fiduciary risk to the Program. They are the following:

(a) The institutional architecture, which remains characterized with too many layers of prior controls and back and forth ex ante review and clearance redundant loops, bureaucratic practices delaying the procurement process. This results in an overall time for the procurement process which exceeds by two to three times the minimum mandatory time per decree regulation).

(b) There is no clear definition of the roles and responsibilities for the follow up of complaints relating to corruption involving procurement. According to article 173 of thePPD, the HICOP is clearly in charge of fraud and corruption cases for what concerns the sanctions and blacklisting part of the procedure (the investigation role is somewhat fuzzy in case of allegation when not transmitted to courts and the distinction between the role of the Investigation Committee – still being implemented - of the High Institution fighting fraud and corruption (INLCC "Instance Nationale de Lutte contre la Corruption" which includes a "Comité d'investigation des cas de corruption et de malversation" and was created in the "décret –loi" No 2011-120 dated November 2011).

(d) The heterogeneous fiduciary capacity of procuring entities with the upper end of the spectrum mostly the large municipalities having strong and developed technical and procurement skills, procurement methods and procedures and at the other end of the spectrum small remote municipalities with low capacity and with low procurement skills. This weakness in procurement capacity could possibly pose a fiduciary risk to the Program. Therefore it is proposed to organize as part of the capacity building component, a systematic baseline assessment of all LG procuring entities using a simplified set of procurement capacity assessment questionnaire. Depending on the questionnaire-based findings, appropriate capacity building support will be designed and provided through the Capacity Building elements of the Program.

29. The assessment of the current program procurement systems for public procurement of Local Governments**,** based on post review during missions of a sample of six cases documented in the archives of CPSCL and from the field visits to selected municipalities it was found that municipalities completed the whole procurement process up to award and signature of the contract much more quickly than national level procuring entities such as line ministries. In fact, the assessment has shown that the overall duration of the procurement process is five to seven months, compared to twelve or more months for central bodies and Ministries. This can be explained by the fact that municipalities/LGs have an annual investment program and are more under direct pressure of local population to actually provide the infrastructure or services needed. Therefore, they may well have more motivation to expedite the procurement process despite the excessive number of prior controls and clearances. In addition, a very high level of compliance with the procedures was found, and very low risk of corruption in LG procurement which is illustrated by the fact that in one full year only one case of noncompliance was detected, and this case is a minor violation of a provision in the decree relating to the constitution of an evaluation committee. Therefore the main procurement risk for the program arises from the slow/sluggish procurement process that results in high overall time for completing the procurement process (five to seven months due to redundant ex

ante controls). Therefore based on the assessment, the Procurement risk for the Program is rated as "***Moderate***".

Governance and Oversight of Program Implementation:

30. Tunisia has a long history of local governance starting with the establishment of the Municipality of Tunis in 1858. There are 264 municipalities and their roles and responsibilities are well defined in the Constitution as well as through various executive orders (*Decrees* and *Arrêtés*). Chapter 7 of the recently approved Constitution lays out clearly the intention of the country to move towards greater decentralization and for a transparent and accountable system of local governance. Municipalities, the lowest tier of the State being close to citizens, are expected to fulfill their mandate to provide local services in a responsive and accountable manner. The Program design is built around this fundamental principle and therefore fits in well with the current priorities of the country to strengthen governance, including participatory governance.

31. *Governance and Oversight of the Local Government System:* LGs in Tunisia report administratively to the DGCPL, within the Ministry of Interior. Administratively, the country is organized under 24 Governorates (Wilayas) headed by a Governor. The Governor, who is appointed by the President, is the representative of the Central Government at the regional level and is responsible for the regional administration including the supervision of the deconcentrated arms of line ministries. The Governor, on behalf of the Ministry of Interior, exercises broad administrative and regulatory supervision over LGs and is the approving authority for LG budgets. In addition, the deconcentrated arms of the line ministries at the Governorate level provide technical and administrative support to LGs in the implementation of programs and projects funded from the Central Government budget on a needs basis.

32. Municipalities are headed by a Mayor who is elected from among town councilors for a period of five years. The Mayor chairs the municipal council and has responsibility for planning, public security, traffic, environment management. The Mayor is assisted by a Secretary General who is the executive head of the municipal administration as well as other technical and financial staff. The Mayor and the Municipal Council are responsible for the day today management of municipal affairs and provide the necessary guidance to and oversight of the executives. The Municipal Council will exercise oversight over the implementation of the municipal plans and budgets that include the Capital grants provided through the Program. The existing Municipal Councils are appointed and elections are scheduled for next year.

33. *Program Governance and Oversight*: The Program will be managed by *CPSCL* under the overall direction of the Secretary General, Ministry of Interior. CPSCL is an autonomous agency created by law (*établissement public non-administratif*) and governed according to the provisions of decree 92-688 of 16 April 1992. CPSCL has its own Board of Directors chaired by the Minister of Interior and its day-to-day management is handled by a Chief Executive. CPSCL in its capacity of Program Manager will exercise Program oversight especially in the implementation of capital investment plans at the municipal level. In addition, CPSCL in its capacity as the lender to municipalities will exercise financial due diligence as part of the review of loan application packages. The roles and responsibilities of CPSCL relating to Program governance and oversight will be described in the Program Operations Manual.

34. The Program is subject to the oversight of existing system of public sector oversight in Tunisia that includes the external audit by the Court of Auditors (*Cour des Comptes*), the inspection by the Inspector General of the Ministry of Interior and the Inspector General of the Ministry of Finance. Though the Constitution has brought about a shift from the stiff ex ante controls imposed by the previous *"tutelle"* system, the day to day operating rules and procedures have not been revised. Therefore, there exists to a large extent the system of process controls imposed by the Ministry of Interior (for example the

budget of municipalities are reviewed by the Governor) as well as those laid out by the country's PFM system for making payments. Thus the recently approved Procurement Decree continues to insist that the adherence of municipalities to procurement rules are verified and approved by the regional branch of the Controller of Expenses (*Contrôle Général des Dépenses*) before contracts can be awarded. Similarly prior approval is required from the Controller of Expenses (*Contrôle Général des Dépenses*) before any payment can be made by the municipality.

35. Independent external audits on an annual basis are an important instrument for ensuring oversight as well as to enforce public sector accountability. In Tunisia the Court of Auditors (*Cour des Comptes*) has the mandate to carry out the external audit of municipalities. However due to internal capacity issues as well as the pressure to complete the audit of the Central Government and its agencies, the *Cour* often found it difficult to conduct the audit of the municipalities on a regular and timely manner. As part of the Program design, it has been agreed with the Court of Auditors (*Cour des Comptes*) that they will carry out annual external audit of municipalities within a reasonable time period after the end of the financial year.

36. *Transparency*: Coming out of a system that was centrally driven ("*tutelle*") and with low levels of transparency, the Governance system in Tunisia is making rapid progress to embed the principle of transparency in the public sector including LGs. The current system of allocation of financial resources from the Central Government LGs is very opaque. The proposals submitted by the municipalities as part of the annual PIC (*Plan d'investissement communal*) process are revised at the discretion of the Ministry of Interior without any consultation or recourse by municipalities. At the municipal level, there is essentially no sharing of information between the municipality and its citizens. At the same time, there are several changes happening at the country level that will help to strengthen overall transparency. A new decree providing Access to Information (Decree # 2011-41) has recently been issued that allows citizens to have easier access to Government documents and records. There are independent initiatives by Civil Society Organizations such as the website called Marsoum41 (http://www.marsoum41.org/en) that provides a platform for access to information. A national Procurement website is a place where all contract awards by public sector entities including LGs are required to be uploaded and thereby making all information relating to contract awards available to the public. The Program intends to build upon these measures and will be strengthening participative planning where the municipality will be required to present the proposed five year and annual plan proposals to their residents in open meetings and obtain public validation of the plans.

37. The Program intends to strengthen transparency through the following specific measures to strengthen transparency:

- Creation of a national level E-Portal that will be populated with relevant geographic, spatial, demographic, financial, service delivery performance data of each municipality.
- Key information relating to the LGs such as financial reports, audit reports, procurement plans, contract awards etc. will be displayed either in the municipal website (if such a website is up and running) and also at a designated place in the municipal offices.
- CPSCL, as the Program Manager will display all relevant information connected with the Program in its website.

38. *Accountability*: The new Constitution has put in place a strong accountability framework for local Governments. The PforR Program reinforces this Constitutional mandate through the unconditional capital grants system that will provide resources to municipalities to be used at their discretion to meet local service delivery responsibilities. Municipalities will be incentivized to prepare Five Year and Annual Plans and Budgets in a participative manner, which will need to be validated by their residents in dedicated public meetings. Municipalities will be accountable to their citizens as well as to the Central Government for meeting their institutional and service delivery responsibilities. The Program will

strengthen downward accountability of the municipality to its citizens, and better reflect citizens' service priorities through the strengthening of citizen participation in the municipality's planning and budgeting process. The Performance Assessment system introduced by the Program will measure institutional performance and will make the results available to the public which will strengthen the accountability relationships between the local Government and its citizens. Formal channels of upward accountability such as regular and timely financial reporting, independent annual external audits will be strengthened under the Program.

39. *Participation*: The extent of public participation in local governance has been very weak in Tunisia partly because of the centralized nature of the State previously. The Tunisian Revolution and the consequent changes resulting in the new Constitution that focusses on decentralization provide a significant fillip to enhanced public participation in local governance. The DGCPL has recently issued a Circular (dated March 7, 2014) where LGs are required to adopt a participative approach and consult with their citizens during the preparation of their five year and annual plans. The Program builds upon the existing momentum in Tunisia on enhancing citizen participation and provides for specific measures such as:

- The five year plans and annual Plans of municipalities will be prepared/finalized after consultation/validation with citizens. This will be part of the Mandatory Minimum Conditions (MMCs) for local Governments to receive the Capital Grants.
- The Program intends to provide incentives to local Governments to introduce participative budgeting in municipalities around a small proportion of their capital investment grants as part of their annual planning and budgeting process.
- The Capacity Building component of the Program will provide training to municipalities to strengthen their communication with citizens and capacity to effectively implement participatory planning and participatory budgeting.

40. *Grievance Handling*: Tunisia has established a system for receiving grievances and their resolution. At the municipal level, each municipality is required to establish a Citizens Relations Bureau, where any citizen can file a grievance on any issue relating to the municipality. Field level assessment has revealed that while the Bureaus exist in many municipalities, their functioning is poor. The Program will provide incentives, via the participatory planning process, for municipalities to strengthen the existing grievance mechanisms, including by ensuring complaints are systematically logged and resolved in a timely fashion under the Bureau's guidance. The grievance log and timely resolution of the complaints will be an indicator for the municipality's performance assessment. The Program Action Plan recommends the establishment of the Bureaus in all municipalities as part of the Program Action Plan. The Good Governance Cell in the Ministry of Interior will monitor the efficiency of grievance handling by the Citizens bureaus and their effectiveness in the resolution of citizens' grievances. The Annual Performance Assessment process will assess the performance of the grievance handling mechanisms.

41. *Complaints Handling*: Citizens can file complaints relating to the municipality directly through the national anticorruption website to the Department of Good Governance and Anticorruption as well as send written complaints to specialized agencies such as the National Authority for Fighting Corruption and to the Good Governance cells maintained by the Ministry of Interior. Complaints can also be filed at the Citizen Bureaus in the municipalities where they are functioning. Those complaints relating to allegations of corruption will be conveyed by the entity receiving the complaint to the National Authority for Fighting Corruption for investigation. Those complaints relating to irregularities in the procurement processes will be conveyed by the entity receiving the complaint to the COSEM for further follow up

action. The CPSCL as Program Manager will be informed by the municipalities regarding the receipt and resolution of grievances and complaints through Program reporting systems.

42. *Specific complaints relating to Procurement*: All complaints relating to the procurements done by the Program including those at the municipal level will be filed with the COSEM that is part of HICOP. As part of the existing system, the municipalities will be publishing all Invitations to Bids in their website and in the local news media and posting all approved contracts in the National Procurement website. Any aggrieved party will have the opportunity to file a complaint within a period of five days after the contract awards are posted in the website. The COSEM will examine the complaints and resolve them with a specified time period. The municipality will keep the CPSCL informed about the resolution of the complaints on a periodical basis .

43. *Assessment of Fraud &Corruption Risks and mitigation*: Though Tunisia is a signatory of the UN Convention Against Corruption (UNCAC) since 2004, the country's record of recognizing and fighting corruption was very weak under the former regime until the Tunisian Revolution in 2011 brought the issue of corruption into center stage. The subsequent changes in the country that built upon the strong public opinion against corruption and favoring good governance have resulted in the setting of a policy and institutional framework for good governance and anticorruption at all levels of Government. This has culminated in the specific provisions included in Article 130 of the country's new Constitution that provides for the setting up of a Commission for Good Governance and Anti-Corruption.

44. *Institutional arrangements for handling corruption and their applicability for the Program*: Tunisia has set up a robust institutional framework for preventing and combating corruption. At the national level, the Department of Good Governance and Anticorruption (*Département chargé de la Gouvernance et de la lutte contre la Corruption*) headed by Secretary of State sets the broad policy framework for governance and anticorruption. As mentioned above, the new Constitution provides for an independent Commission for Good Governance and Anticorruption composed of independent impartial members and who shall be in charge of monitoring cases of corruption within the public and private sectors, investigating and confirming them, and submitting them to the relevant authorities. Steps are currently on for providing institutional form to this Constitutional provision.

45. The Department is currently in the process of preparing a National Strategy for preventing and combating corruption with the support of UNDP. As part of its efforts to strengthen transparency and good governance the department has set up a website called http://www.anticor.tn/ that provides a platform to bring together the main national stakeholders committed to anti-corruption by being more open and transparent to civil society organization and citizens' contributions and provides a repository of laws and decrees relating to anticorruption as well as articles and documents relating to good governance and anticorruption. The Department of Good Governance through circular # 16-2012 (March 2012) has required all line ministries, Governorates and public institutions to set up a cell for good governance under the supervision of the head of the organization.

46. The Fiduciary Systems assessment revealed that even though good governance cells have now been established in most line ministries at the Central level, they have not been established and functional at the municipal level. The Program recommends the setting up of the good governance cell in all municipalities as part of the Program Action Plan.

47. The National Authority for Fighting Corruption (*Instance Nationale de Lutte contre la Corruption*) is responsible for the investigation of complaints and for taking follow up action. Established by Article 12 of the Decree 2011-120 of 14 November 2011, the authority is composed of its president, board, general secretary and the prevention and investigation committee. The National Authority is

administratively under the Department of Good Governance and Anticorruption, and is headed by a President and comprise of twenty staff. The Authority is empowered to receive and investigate corruption allegations in all public and private organizations and includes municipalities in their scope. The Authority receives complaints either through the national anticorruption website (www.anticorruption-idara.gov.tn) directly through mail. According to Article 34 of the Decree referred to above, it is obligatory for local Governments to report any allegations/complaints of corruption to the National Authority. The National Authority for Fighting Corruption is in the process of setting up of a national portal for complaints and for reporting corruption cases called "E-People" to better manage, track and collect complaints and corruption allegations. In addition to the above, there are initiatives by civil society organizations that provide a platform for citizens and civil society to bring issues relating to corruption into the public domain.

48. After a preliminary scrutiny of the complaints, the Authority carries out detailed investigations of credible complaints to establish whether there is a prima facie case of corruption involved. Once a prima facie case is established, the Authority transfers the case to criminal investigation authorities for initiating prosecution steps under the Criminal law of the country. Though the Authority is making serious efforts to provide speedy resolution, the huge backlog of cases (relating to the previous regime) has reduced the Authority's ability to process new complaints quickly. The Authority is currently in the process of addressing this issue through donor support. The Authority is also working together with the Department of Institutional Integrity (INT) of the World Bank. It is expected that an agreement will be signed soon to exchange information and experiences between the two organizations as well as for joint investigations and capacity building.

49. The complaints handling and processing systems of the Authority are found adequate for the purposes of the PforR operation. It was discussed and agreed with the Authority that complaints relating to the Program, if any, will be conveyed to the Authority by the municipality or any other entity receiving the complaint. The Authority will take steps to investigate the complaints expeditiously in accordance with its procedures and convey the results of the investigation through a report to the Secretary General, Ministry of Interior who will in turn share the report with the World Bank. In accordance with the INT guidelines for PforR operations, if any further follow up investigations are required, the Bank will rely on the Authority to carry out such investigation and will rely on the findings of such investigation for initiating any follow up action. The Program will provide specific support to the Authority for carrying out specific investigations in an expeditious manner through consultant and/or logistical support as necessary, which will be organized by CPSCL. The Program Operations Manual will describe the procedures for the conveyance of complaints and the sharing of the investigation results in detail.

50. *Debarment of Contractors*: In accordance with the INT guidelines for PforR operations the Program will take steps to ensure that "any person or entity debarred or suspended by the Bank is not awarded a contract under or otherwise allowed to participate in the Program during the period of such debarment or suspension". At the conclusion of the procurement process for each contract and prior to the award of the contract, each municipality will publish the details of the contract award in the national public procurement portal. CPSCL will verify the names of the contractor against the World Bank's database (www.worldbank.org/debarr) of debarred or suspended contractors to ensure that no such contractor is awarded any contract under the Program. CPSCL will convey the results of the verification to the municipality within the "standstill period" of five days from the publication of the contract award.

Program Implementation, Audit and Disbursements:

51. CPSCL will be the tdesignated to coordinate the implementation ofthe PforR Program and will be responsible for the disbursement of the Capital Grants to municipalities as well as for the management of

the capacity building support provided under the Program. CPSCL will also be responsible for preparing the Program Financial Statements compiling them from municipal financial reporting as well as financial reporting from other agencies, if any. The protocols for the receipt and compilation of annual Program financial statements will be defined in the Program Operations Manual. The annual audit of the Program financial statements will be carried out by the Court of Auditors (*Cour des Comptes*). The Terms of Reference for the audit will be part of the Program Operations Manual.

52. *Program Fiduciary Risk Assessment:* Based on the assessment, it is concluded that the Program Fiduciary Systems have the capabilities to provide reasonable assurance that the financing proceeds will be used for intended purposes. However, there are significant gaps and weaknesses in these systems which need to addressed as part of Program implementation. These gaps and weaknesses have the potential to make the fiduciary risk of the Program to be high thereby impacting the ability of the Program to achieve its intended results. Therefore, a Program Action Plan was prepared based on the findings and conclusions of the Fiduciary Risk Assessment that will mitigate to a large extent the fiduciary risks and weaknesses identified. Considering the existing weaknesses in Program Fiduciary systems and the time and effort required to implement the Program Action Plan and the capacity building initiatives, the residual fiduciary risk rating for the Program is rated as **Substantial**.

Annex 6: Environmental and Social Systems Assessment Summary

Introduction

1. The following annex summarizes the findings of the Environmental and Social Systems Assessment (ESSA) undertaken for the proposed operation. The following sections will (i) describe the ESSA process; (ii) describe institutions, roles, responsibilities, and coordination; (iii) outline the main environmental and social effects of the Program activities; (iv) discuss the assessment of the Program's legal and regulatory framework for environmental and social management vis-à-vis World Bank requirements for Program-for-Results financing, and assesses capacity and performance of Program institutions to meet those performance requirements; and (v) outlines actions to strengthen Program systems. Broadly, the ESSA concluded that the social and environmental arrangements under the Program are appropriate for financing.

2. The ESSA examines the Program's systems for environmental and social management for consistency with the standards outlined in OP/BP 9.00 (*Program-for-Results Financing*) with an aim to manage Program risks and promote sustainable development. Paragraph 8 of OP 9.00 outlines what the ESSA should consider in terms of environmental and social management principles in its analysis. Those core principles are:

3. Environmental Management Systems:
   - Promote environmental and social sustainability in the Program design; avoid, minimize, or mitigate adverse impacts, and promote informed decision-making relating to the Program's environmental and social impacts;
   - Avoid, minimize, or mitigate adverse impacts on natural habitats and physical cultural resources resulting from the Program; and
   - Protect public and worker safety against the potential risks associated with: (i) construction and/or operations of facilities or other operational practices under the Program; (ii) exposure to toxic chemicals, hazardous wastes, and other dangerous materials under the Program; and (iii) reconstruction or rehabilitation of infrastructure located in areas prone to natural hazards.

4. Social Management Systems:
   - Manage land acquisition and loss of access to natural resources in a way that avoids or minimizes displacement, and assist the affected people in improving, or at the minimum restoring, their livelihoods and living standards;
   - Give due consideration to the cultural appropriateness of, and equitable access to, Program benefits, giving special attention to the rights and interests of the Indigenous Peoples and to the needs or concerns of vulnerable groups; and
   - Avoid exacerbating social conflict, especially in fragile states, post-conflict areas, or areas subject to territorial disputes.

5. The ESSA considers the consistency of the Program systems with these principles in two ways: (i) as systems are defined in laws, regulation, procedures, etc. (the "system as written"); and (ii) the capacity of Program institutions to effectively implement the Program environmental and social management systems (the "system as applied in practice"). This annex describes a gap analysis between the Program principles and Tunisian systems on both levels.

ESSA Process

6. Preparing the ESSA and developing measures to strengthen the system for environmental and social management has benefitted from a broad range of inputs and an extensive consultation process. This has included:

7. **Field visits**: Visits to about ten Municipalities to establish the status and standard of environmental and social safeguard systems at the municipal level and interviews with technical staff in relevant institutions within the Government and Development Partners;

8. **Desk review:** The review covered current environmental and social legislations and regulations, relevant environmental and social reports (e.g. ESMF and RPF), and distinct reports on the implementation of the previous and ongoing World Bank municipal development projects, including t the ongoing Tunisia Urban Technical Assistance Program;

9. **Initial consultation meetings:** Meetings were held with technical staff in municipalities, Regional councils, and other ministries and Government institutions, including ANPE, Ministry of Equipment, Territorial Management, and Sustainable Development, the Urban Renovation and Rehabilitation Agency (ARRU), the National Sanitation Utility (ONAS), the National Waste Management Agency (ANGED), and CFAD to develop understanding of procedures, standards, and approach. A list of personnel involved in this consultation will be contained in the ESSA Annexes;

10. **Validation workshop**: a consultation workshop took place on April 16, 2014, with government technical staff (at national, regional and municipal levels) and development partners. The draft ESSA report was circulated prior to the meeting. Observations from the workshop have been incorporated into the ESSA report and a complete list of participants and a summary of their comments is included in Annex 3 to the ESSA (Stakeholder Consultation Workshop).

11. **Document dissemination**: The draft final ESSA report was publically disclosed through the World Bank's Infoshop on May 15, 2014, and advertised through the World Bank Tunisia web page, and public comments were solicited during a one month period reserved for comments.

Institutions, roles, responsibilities, and coordination

12. Under the Program, the main institutions involved with environmental and social management are as follows:

13. **The CPSCL** will have the primary responsibility of managing the grant allocation and local governance performance monitoring systems and will be responsible for day to day management and monitoring of the Program in line with the Program implementation schedule. CPSCL will be also in charge of reporting to the Bank on Program implementation progress and will ensure compliance of the sub-projects (preparation and implementation) with environmental and social requirements and standards; it will also be required to verify at each step that the conditions for granting funds are met.

14. **Municipalities** are responsible for preparing the interim and detailed applications for Grant and loans. They will ensure compliance with environmental and social measures during Program implementation. To comply with the system, municipalities generally rely on consultants to investigate and prepare various reports and project documents (preparation and monitoring of environmental assessments, technical studies, work reception, technical assistance contracts, operational structures, etc..) which they submit to the CPSCL for review and approval prior to obtaining loans or grants agreements and disbursement of funds. In addition to implementing the investments that UDLGP will

support, the municipalities are responsible for development planning and, depending on the project, at times responsible for oversight of environmental impact management within their boundaries. The key person for environmental management is the Municipal Environmental Officer; this role is in general assigned to a technical staff with very weak environmental capacities. The municipalities are also at the center of land acquisition for UDLGP activities.

15. **The Agence Nationale de Protection de l'Environnement (ANPE)** was created by Law No. 88-91 of August 2nd 1988. It is administered by a Governing Board chaired by a Director General, appointed by decree on a proposal from the Ministry in charge of sustainable development. In addition to its central structures, the ANPE is represented at the regional level by eight representations. This institution acts as the principal agency in Tunisia for the management of the environment. As such, the ANPE coordinates, monitors and supervises all activities in the field of the environment and many elements of natural resource protection. ANPE coordinates the process of Environmental Impact Assessment, reviews EIAs and issues certificates of approval, monitors and enforces compliance with environmental standards and with the conditions contained in certificates of approval for EIAs, and has promulgated general guidelines for EIA as well as EIA guidelines for specific economic sectors and is currently in the process of updating them.

16. **The National Office of Sanitation (ONAS)**, a public institution with industrial and commercial character, was created in 1974. Its preliminary responsibility is the management of the sanitation sector and the protection of the water environment in the 165 municipalities where it currently operates (with a connection rate of 90 percent). ONAS ensures the operation, maintenance and renewal of any infrastructure related to sanitation of cities such as wastewater treatment plants, sanitation networks, pumping stations etc. In the context of this program, ONAS will assist municipalities in the preparation and approval of sanitation studies, the acceptance of works and the use of the infrastructure supported by the program;

17. **The Rehabilitation and Renewal Agency** (**ARRU**[45]) was founded on August 1st, 1981 by Law No. 81-69. The ARRU was entrusted by the Government with the role of public operator for rehabilitation and urban renewal in Tunisia. As a delegated contracting authority, ARRU has worked for 30 years against the exclusion of popular neighborhoods from sustainable urban development. Project management is entrusted to the ARRU for the achievement of technical and socio-economic studies, land clearance, contract management, and the coordination and monitoring of the entire project. These activities are performed by operators led by ARRU or delegated to it, ARRU uses consultants and construction companies services.

18. Other institutions potentially involved in environmental and social management of activities under the Program include:

19. **Regional Councils**: The *gouvernorat* is a public entity with independent administrative status and financial autonomy, that is managed by a regional council that is notably responsible (under the Organic law on Regional Councils) for oversight of regional projects, supporting cooperation between communes and supervising the implementation of projects jointly managed by communes.

20. **The Centre for Training and Support to Decentralization (CFAD)**: According to its founding law, the Centre is a public entity with an administrative character, with a public responsibility and financial autonomy. Its mandates include upgrading and training administrative staff of regional councils, municipalities, as well as the selection and upgrading of trainers. The Center can enter into fee-

[45] Agence de Réhabilitation et de Rénovation Urbaine

based service agreements and contracts with national or international parties for services that are covered by their mandates.

Program environmental and social effects

21. While UDLGP funds are based on community priorities, there are criteria for what can be financed from a list of core municipal services including small- to medium-scale civil works such as roads and paving, construction, rehabilitation and upgrading, street lighting, sewerage extension/connection to public network, storm water drainage, solid waste collection, parks and some recreation facilities, markets, and other environmental improvements (see Annex 1 for detailed Program description).

22. The ESSA analyzed the Program activities for the level of potential impacts. This analysis concluded that because the types of activities to be financed by the Bank are intended in part to remedy environmental degradation and social issues linked to rapid urbanization, their overall effect should be positive, though adverse environmental and social impacts are possible. Based on the type, scope and scale of works allowable under UDLGP, adverse impacts are expected to be typical construction impacts that are site-specific and generally limited to the construction phase. Similarly, given the scope of activities under the program it is unlikely that involuntary resettlement should be required, although small-scale land acquisition is possible for the construction of infrastructure works, for example in widening roads in the existing rights-of-way or acquiring land for new market areas. This has the potential to impact land, assets, property, crops, and shared community facilities such as water points, community roads, and roadside markets. Because of the significant geographic dispersion of the participating municipalities and the scale of proposed investments, cumulative effects of the Program as a whole are unlikely.

23. While no large-scale or high-risk projects are expected, the screening process in the Program Operations Manual will have criteria to exclude certain categories of projects as well as projects of a scale that would include significant negative impacts that are sensitive, diverse, or unprecedented on the environment and/or affected people. Such types of investments are excluded from the Program (per OP/BP 9.00). In addition to screening for significant impacts, the following exclusionary criteria apply to works financed under UDLGP, which will be included in the POM’s screening criteria:

- Wastewater treatment plants,
- Landfills and waste transfer stations,
- Slaughterhouses,
- Activities that would significantly convert natural habitats or significantly alter potentially important biodiversity and/or cultural resource areas, and
- Activities that would require the relocation of residential households or commercial activities and/or significant involuntary land acquisition.

Assessment of Environmental Management Systems

24. Projects currently implemented by LGs primarily employ Tunisian systems for environmental and social management; and these were assessed by the ESSA. The ESSA conducted an analysis of existing systems for environmental and social management for consistency with the core principles of OP/BP 9.00, described above. The complete list of findings is outlined in detail in the ESSA, with the main gaps summarized below.

25. **Current Environmental and Social Management Framework**: Previous World Bank projects, and mainly the third Municipal Development Project have led to the adoption of Bank systems and screening procedures by the CPSCL and the municipalities. The ESSA found that in general, the

Tunisian system for environmental and social impact assessment is well established and relatively comprehensive, reflecting international practice, and are in many ways consistent with the core principles of OP 9.00. However, there are some areas that need further strengthening.

26. Due diligence and oversight of the impact assessment process for projects with lower levels of environmental risk are typically handled by CPSCL and municipalities and, while projects requiring full Environmental Impact Assessments are handled by ANPE at the central level. Most projects under UDLGP would be classified for CPSCL and local Government oversight, which is where the ESSA focused the assessment of current performance.

27. **System strengths**: The ESSA found a number of positive developments in how the existing system has been working and able to deliver improvements to the system for environmental and social impact assessment. Under the PDM III, the CPSCL prepared (i) a practical guide for investment projects in local collectivities (April 2003) which includes procedures for Environmental Assessment; and (ii) Draft Resettlement Guidelines (2013). These documents define the steps and procedures for the environmental management of the planned activities, and allow to screen projects for environmental impacts, and to ensure that environmental assessments are carried out and mitigation actions are identified for environmental issues. Social assessments are not part of this process, although this is not yet well advanced in implementation. Regular reporting requirements allow the CPSLC to ensure that existing systems are implemented, although some overarching issues can be identified that still lead to underperformance: i) human resource gaps at various levels; ii) financial resources constraints at all levels; iii) the absence of social impacts assessment; (iv) the absence of public and affected populations consultation; and (v) the absence of disclosure of EIA documents. There is also a need to update the CPSCL's guide for investment projects in local collectivities which is over ten years old, particularly with regards to project screening, public consultations and disclosure and environmental supervision and monitoring.

28. Initiatives on environmental and social planning have started to improve and strengthen systems. There is now a clear need to ensure that further support to the ANPE, the CPSCL and to the municipalities leads to the achievement of observable and measurable results by following through from the planning stage through project implementation to identify and minimize impacts, and maximize the environmental and social benefits arising from municipal infrastructure projects.

29. **Gaps in the system**: The principles pertaining to environmental systems under OP/BP 9.00 are considered in terms of environmental and social management for urban municipal infrastructure projects that are implemented by municipalities. In general the assessment finds that the regulatory environment in Tunisia is reasonably well developed and articulated with respect to environmental parameters. However, several gaps in the system that were identified in the ESSA are outlined below:

- **Screening and Categorization:** The revision of the 1991 EIA Decree in 2005 did certainly introduced some improvements (simplification of procedures for the preparation and approval of the EIA system) but in has eliminated the possibility of submitting some projects as appropriate to the environmental assessment and therefore increased risk in relation to the categorization and projects screening. This revision also limited the scope of the environmental impact analysis components by removing the legal provisions relating to socio-economic impacts.
- **CPSCL guide** for investment projects in local collectivities (April 2003) was established under the 1991 decree; and it is now not in conformity with the new 2005 EIA decree. The revision of this guide in relation to the new legislation will address issues related to the screening and categorization mentioned above.
- **Social assessment:** Social issues, including identifying and mitigating impacts on vulnerable groups in municipalities, are often missed or understated given a lack of clear guidance and/or staff specialized in this area.

- **Grievance and redress mechanisms (GRM):** Most municipalities do not have a formal system for handling complaints. Consultations conducted confirmed that the way to deal with grievances is mostly informal and unstructured. A standardized Grievance resolution process should be in place to take into account complaints and resolve conflicts in a timely and appropriate manner. Municipalities participating in the Program will need to adopt effective grievance and redress mechanisms.
- **Consultation and Disclosure:** For all projects handled through ANPE or municipalities, there is no process for consultation or disclosure required by law. The CPSCL guideline also does not include clear consultation and disclosure mechanism.
- **Monitoring:** Regular monitoring of project implementation to ensure that EMPs are carried out is particularly problematic at all levels. Approximately, less than 50 percent of project requiring EIA are being monitored by ANPE due to lack of financial resources and personnel. The municipalities' technical staff in charge of the environment often does not have the qualifications nor the budget to ensure the monitoring of the EMPs; they generally rely on consultants to investigate on a case by case basis, and prepare environmental monitoring reports submitted to the CPSCL for disbursement of funds.
- **Resource constraints:** The CPSCL has the technical expertise necessary to run the program at central level, but municipalities' lack of trained officers with necessary skills to carry out environmental and social assessment. In the municipalities, the concept of environment is confined to the concept of environmental health and sanitation, in particular refuse collection, street cleanliness, hygiene and health. Environmentalist function does not exist per say in the municipalities as a function, this task is often attributed to a technical staff when it is required by a development partner, but that person has neither the qualifications nor the understanding of what it was asked to do. Also the lack of funding for assessment, consultation, monitoring and evaluation is a key constraint.
- **Training:** While the CPSCL has prepared a set of technical tools including Environmental Assessment Guidelines (2003) and Resettlement Guidelines (2013) for environmental and social management in local Governments, there has been limited training to help disseminate these tools. The municipalities' technical staff have received some training on the procedures they are required to follow, but the fact that there is no structure officially in charge of the environmental and social management has resulted in the absence of capitalization of experiences. When trained personnel leave, there is no longer capacity. This affects the sustainability of capacity building actions.

Assessment of Social Management Systems

30. **Land acquisition and resettlement:** Projects currently implemented by municipal local Governments should adhere to Tunisia's land laws, with projects financed by the World Bank using Resettlement Policy Frameworks (RPFs) and Resettlement Action Plans (RAPs), both of which were assessed through the ESSA for consistency with the core principles of OP/BP 9.00 (described above). The ESSA found few gaps between the Tunisian system and Program requirements - the complete findings are outlined in detail in the ESSA, with the main gaps summarized below.

31. Property rights are a fundamental right defined and guaranteed by the Tunisian Constitution and the Code of Real Rights (*Code des droits réels*) which states: "No one may be forced to sell his property except in cases provided by law (expropriation for public utility), subject to fair compensation " (Article 20). Expropriation is applied by the State for public utility, in specific cases (Law n ° 2003-26).

32. Legislation on expropriation for public utility does not include explicit provisions for loss of income, livelihoods, and restriction of access to material, goods and natural resources (economic resettlement). Some of these aspects, however, are governed by other laws that guarantee the right to access, use of water and natural resources, but not in the context of the acquisition of land (Water Code, Forest Code, ATU code, etc.).

33. From a social perspective, gaps and weaknesses are mainly related to involuntary resettlement, as well as to participation and social accountability practices. Municipalities will need to ensure that people affected by loss of land and assets – in the unlikely event where this should occur in the context of basic infrastructure sub-projects – are properly compensated and assisted in the restoration of their livelihoods. This will require upgrading of the CPSCL's draft Resettlement Guidelines (*Plan cadre d'acquisition de terrains*, 2013) and providing appropriate guidance to municipalities, particularly in regards to the resettlement and compensation of non-authorized commercial occupants of public lands and rights-of-way. Municipal representatives that were consulted during the Pre-appraisal mission expressed a need for guidelines for the resettlement of non-authorized occupants of public lands and rights-of-way, given that the revolution and its aftermath had led to a number of spontaneous occupations of public lands.

34. Guidance on citizen engagement in development investments and activities and on the use of grievance and redress mechanisms is also lacking. Importantly, attention needs to be paid to improving the transparency and accountability of implementing organizations. Guidelines need to be developed for effective participation and consultation with affected residents. Municipalities participating in the Program will also need to adopt effective grievance and redress mechanisms.

35. **Indigenous Peoples and vulnerable groups:** OP/BP 9.00 requires that due consideration be given to cultural appropriateness of, and equitable access to, program benefits giving special attention to rights and interests of Indigenous Peoples and to the needs or concerns of vulnerable groups.

36. With regards to Indigenous Peoples, the ESSA undertook a screening of the Program area for recognized ethnic minority groups in Tunisia: The Berber-speaking minority is a very small community living mainly in isolated pockets in southern Tunisia. The Government claims that Berbers have been integrated into Arab Muslim culture and do not constitute an autonomous localized minority of specific character. Because of this, it is difficult to find reliable statistics or evaluate the Berber situation, but they do not appear to have faced widespread discrimination or developed any opposition to Government as in a few other countries of North Africa. In consideration of the fact that the scope of the Program is limited to urban municipalities rather than to rural areas where issues related to the presence of recognized ethnic minority groups could arise, the ESSA confirmed that this social issue is not applicable to the Program.

37. With regards to vulnerable persons, the ESSA did not lead to the identification of specific groups of vulnerable persons that might be affected by the Program. The design of the Program, and in particular its Local Governance component, aims to foster the integration of vulnerable groups such as women and the youth into the national decentralized development agenda through the development of appropriate social accountability mechanisms.

38. **Social conflict:** OP/BP 9.00 seeks to avoid exacerbating conflict, especially in fragile states, post-conflict areas, or areas subject to territorial disputes. Even if the country is in a post-revolutionary context, Tunisia is not considered a fragile state, a post-conflict area, or an area subject to territorial disputes. Accordingly, this social issue is not really relevant to the Program. However, while there is little risk that the Program will be the source of social conflict, some cases of conflict and grievances may occur during Program implementation (such as disputes over land tenure, resettlement, and/or induced impacts). Where grievances and disputes arise in projects, vulnerable groups are frequently unable to access the legal system due to the financial burden and therefore have no access to arbitration should appeals to the local Municipal Council fail. The design of the Program, and in particular its Local Governance component, aims to foster the minimization of social conflict through the development of appropriate municipal public consultation and grievance redress mechanisms.

Measures to Strengthen Systems for Environmental and Social Management

30. While the environmental and social risks of the activities under the Program are low - to moderate-impact, the Program modality offers an opportunity to strengthen both the gaps in procedures identified above in order to identify and mitigate impacts, but also to strengthen the overall system in three areas: (i) strengthening the foundation for environmental and social management, (ii) ensuring implementation of good environmental and social management; and (iii) providing oversight of environmental and social management. To address gaps identified by ESSA, the Program will support specific measures for strengthening the performance of Tunisia's environmental and social management system. These measures are through several mechanisms that are built into the Program through the following mechanisms:

- **Environment and Social Guideline (ESG):** The ESG will be used by LGs in assessing and managing environmental and social impacts and land acquisition. This guideline will build on existing guidelines (the 2003 Environmental Guidelines and the 2013 draft Resettlement Guidelines) and strengthen procedures currently implemented to ensure consistency with the core principles of OP/BP 9.00 and Tunisian laws. The Program Performance Assessment has significantly raised the profile of environmental, social, and land acquisition issues through the inclusion of minimum conditions for core staff and ensuring that a functional system is in place and operational.

- **Capacity Building:** Measures for environmental and social management are integrated in the Program through the Capacity Building and Technical Support Component that allows local Governments to access formal training. CPSCL will provide guidance to municipalities for the formulation and execution of their capacity building plans, as well as a limited amount of supply driven capacity building support to municipal LGs**.** One of the key areas that are eligible for capacity building support in the municipalities is to improve municipal LG's capacity in environmental and social management, supervision of projects – the types of activities include tooling, formal and informal training, mentoring, and on-the-job training.

Together, these form the ESSA Action Plan, which recommends measures that are embedded in the overall Program design through the mechanisms described above. Implementation by municipalities of the environmental and social procedures defined in the Program Operations Manual will be one of the criteria selected for the Performance Assessment System set up..

31. Some actions are further strengthened by inclusion in the overall Program Action Plan which is agreed with the Government, and/or legally covenanted in the Program Financing Agreement. Actions are grouped into three areas:

1. Actions to strengthen the **foundation** of an environmental and social management system
2. Actions to strengthen **implementation and oversight** of that system
3. Actions to **build capacity** in environmental and social management.

Area 1: Strengthen foundation				
No.	**Measures**	**Mechanism**	**Responsible**	**Timeframe**

1.1	ESG developed that provides and include (i) procedures for environmental and social management for LGs updated to address gaps found in ESSA; (ii) social assessment; (iii) public consultations, (iv) screening updated to include guidance to identify high-risk activities, which are ineligible for Program support ….	ESG	CPSCL	Prior to Program effectiveness
1.2	**Revision of the EIA decree** The ANPE aims to revise the EIA Decree to fill identified gaps in the current system, but it is unlikely that the draft decree will be prepared and promulgated before start of the Program. In this respect, it is proposed to support the ANPE through the Program to achieve the following activities: - provide technical assistance to revise the EIA Decree - Reinforce through training ANPE staff in charge of EIAs on screening and categorization, social impact assessment, public consultation and disclosure. - Support the development of specific tools for project oversight and monitoring - Involve the ANPE in the assessment and monitoring of the UDLGP funded projects ANPE will support the program by: - using its experience and expertise to support CPSCL and municipalities to better manage the environmental and social issues of the program and comply with the relevant procedures included in the technical guide - Ensure with the Ministry in charge of the Environment the approval of the revised EIA Decree during the two first years of the program		ANPE	Before Program Year 3
1.3	All Municipal LG's required to have position of Environmental and Social Management Officer substantively filled	APA (Performance Indicator)	Municipal LGs	Prior to Program effectiveness
1.4	All Municipal LGs establish a Complaints Handling Mechanism that will include procedures for environmental, social, and land acquisition, resettlement and compensation issues, as well as fiduciary issues	APA (Performance Indicator)	Municipal LGs	Before Program Year 1
1.5	ESM illustrates required consultation and disclosure of key documents for environmental and social due diligence, and screening form must indicate date and place of disclosure of the environmental and social documents.	ESM	Municipal LGs	Prior to Program effectiveness
1.6	Set up monitoring system for LGs, that tracks, for example, land acquisition, risk, consultations, etc.	ESM	CPSCL	Before effectiveness

Area 2: Implementation and Oversight				
No.	**Measures**	**Mechanism**	**Responsible**	**Timeframe**
2.1	Municipalities consider environmental and social impacts in prioritizing development projects	POM	CPSCL / Municipal LGs	Throughout Program
2.2	All infrastructure projects required to have completed Environmental and Social Screening Form and receive necessary endorsement	ESM	CPSCL/ Municipal LGs	Throughout Program
2.3	Environmental and Social Management Plans are made publicly available at the Municipal Council office and on-site by contractors	APA (Performance Indicator)	Municipal LGs	Throughout Program
2.4	Municipalities' technical staffs in charge of the environment carry out monitoring and supervision of works at least once per quarter.	APA (Performance Indicator)	Municipal LGs	Throughout Program
2.5	Land Acquisition procedures applied and implemented for all projects where the Environmental and Social Screening indicates land acquisition will be necessary, including payment of any compensation prior to initiating works.	ESM/APA (Performance Indicator)	Municipal LGs	Throughout Program
2.6	Reporting from municipal LGs to CPSCL will include tracking grievances related to environmental and social management and land acquisition/valuation.	ESM	CPSCL / Municipal LGs	Throughout Program
2.7	All mitigation measures for environmental, land (where necessary) and social issues for previous CY have been effectively executed.	APA (Performance Indicator)	Municipal LGs	Throughout Program
2.8	Reporting on environmental and social criteria included in Impact Monitoring Reports prepared by the municipal engineer or physical planner	ESM	Municipal LGs	Throughout Program
2.9	Assess that mitigation measures are being followed when projects are implemented.	APA (Performance Indicator)	Municipal LGs	Throughout Program
Area 3: Capacity and Oversight				
No.	**Measures**	**Mechanism**	**Responsible**	**Timeframe**
3.1	Environmental and social management included as a key eligible area for capacity building support	Capacity Building Plan	CPSCL / LG	Throughout Program
3.2	Program Capacity Building includes resettlement as one of the key thematic areas for institutional improvement, both at the municipal and national levels.	Capacity Building Plan	CPSCL	Throughout Program
3.3	Training program will build capacity of core environmental and social staff, but also provide sensitization on environmental and social issues for other technical staff in the municipal LG and Council leaders.	Capacity Building Plan	CPSCL / LG	Throughout Program
3.4	Training program includes session on budgeting for environmental mitigation measures. This will be expanded to include budgeting for land/asset/livelihood compensation.	ESM	CPSCL	After Year 1

3.5	LG training will include screening for land acquisition, impacts on assets and livelihoods as well as considerations for vulnerable groups.	ESM	CPSCL	Within first year
3.6	LG training program for environmental management will be reviewed and updated	ESM	CPSCL/ LG	One year after effectiveness
3.7	Training program on environmental and social management for LGs will include greater instruction on consultation, transparency and handling grievances.	ESM; Agreement	CPSCL/ LG	One year after effectiveness

Annex 7: Integrated Risk Assessment

<table>
<tr><td colspan="5">1. PROGRAM RISKS</td></tr>
<tr><td>1.1 Technical Risk</td><td>Rating:</td><td colspan="3">Substantial</td></tr>
<tr><td rowspan="2">Description:
Limited LG’s capacity to execute investment plans. The Program’s implementation arrangements involve a significant transfer of responsibility to the LGs in terms of identification, preparation, and execution of specific investment subprojects.

Sustainability of infrastructure investments can be affected by weak technical design and/or insufficient O&M expenditure subsequent to asset creation.</td><td colspan="4">Risk Management : The Program adopts a two-pronged approach to strengthening the LG’s capacity to prepare and execute their annual investment plans.

First, the Program will include a comprehensive capacity component through which LGs will be provided to technical assistance and capacity building on a demand basis. Specific technical assistance and capacity building packages will be developed to provide LGs with the tools required to meet their increased responsibilities.

Second, the Program will provide incentive to LGs through the introduction of an Annual Performance Assessment, which results will be published on an annual basis and will determine each LGs access to capital grants.

The CPSCL will contract consulting firms to provide LG with just-in-time technical assistance with focus on the targeted performance areas. This is in addition to the training program managed by CFAD and targeting technical and administrative staff of LGs.</td></tr>
<tr><td>Resp: Government at all levels</td><td>Stage: Imp</td><td>Due Date : CY 15</td><td>Status: Ongoing</td></tr>
<tr><td>1.2 Fiduciary Risk</td><td>Rating:</td><td colspan="3">Substantial</td></tr>
<tr><td rowspan="3">Description :
Transition from the existing system of ex-ante controls operated by the CPSCL to a decentralized system relying on (i) participatory planning and budgeting, (ii) ex-post controls relying on existing institutions and systems, and (iii) public disclosure of information on technical and financial aspects of LGs capital investment .</td><td colspan="4">Risk Management :
- Revision by the CPSCL of the existing procurement guideline for the implementation of investments projects by LGs to move from the existing system of ex-ante control and clearance to post-review. .</td></tr>
<tr><td>Resp: CPSCL</td><td>Stage: Prep</td><td>Due Date : Effectiveness</td><td>Status: Ongoing</td></tr>
<tr><td colspan="4">-Annual audit of local Governments being introduced with the objective of having independent external audit of local Governments carried out in a regular and timely manner

- Mandatory Minimum conditions include conditions relating to compliance with fiduciary practices such timely preparation of budget and financial statements, annual investment plans and procurement plans
(- areas relating to transparency, accountability, and participation in the LG Annual Performance Assessment framework.

- Consolidated program financial statement to be prepared by CPSCL and audited by the Court of Auditors.</td></tr>
</table>

	Resp: Government	**Stage:** Imp	**Due Date :** Recurrent	**Status:** Not yet due
1.3 Environmental and Social Risk	**Rating:**	**Moderate**		
Description : While the overarching legal and institutional framework for environmental and social management is adequate, lack of specific guidance and local capacity can lead to uneven implementation at the LG level.	**Risk Management :** **-** Revision and updating of the existing Environment Guidelines and Resettlement Guidelines by the CPSCL.			
	Resp: CPSCL	**Stage:** Prep	**Due Date :** Effectiveness	**Status:** Ongoing
	- Specific training to be offered to LGs as part of the Program's Capacity Building component in order to strengthen LG's awareness and capacity for implementation of the Program's provision in terms of environmental screening and assessment of investment projects, environmental monitoring and supervision, community participation in sub-project design, and social management.			
	Resp: CFAD	**Stage:** Imp	**Due Date :** CY 15	**Status:** Not yet due
1.4 Disbursement linked indicator risks	**Rating:**	**Moderate**		
Description : Whereas performance assessment is a central element of the Program, the introduction of the LG performance assessment system is only envisaged in the third year of the Program.	**Risk Management :** Mandatory Minimum Conditions are introduced from the first year of the program. The CPSCL will verify the compliance of LGs with the Program's minimum conditions which will determine the LGs' access to Capital Block Grants. This implementation arrangement will be dovetailed with the initiation of the Annual Performance Assessment in CY 2016 of the program and its use as the main platform for monitoring the performance of the LGs from CY 2017.			
	Resp: Government	**Stage:** Imp	**Due Date :** CY 15	**Status:** Not yet due
2. OVERALL RISK RATING : High				

Legend: L – Low
M – Moderate
S – Substantial
H – High

Annex 8: Program Action Plan

Action Description	Due Date	Responsible Party	Completion Measurement	Link to DLI	Covenant
Results Area 1 – Transparent Capital Grant System					
1. Decree 97-1135 replaced to introduce transparent formula based allocation of capital grant for municipal infrastructure delivery	Effectiveness	MoI and MoEF	The revised decree has been approved	DLI 1	[ ]
2. Ministerial Decree issued indicating the annual allocation formula and MMCs applicable to capital grant for municipal infrastructure delivery	CY 14	MoI	The Ministerial Decree has been issued	DLI 2	[ ]
Results Area 2 – Municipal Performance Assessment					
3. Preparation and approval of the LG Performance Assessment Manual and training for CGSP	CY 15	CPSCL	The LG Performance Assessment Manual has been approved	DLI 4	[ ]
4. E-portal designed and operational	CY 15	CPSCL	E-Portal has been populated with existing data and is accessible to the public	DLI 8	[ ]
Results Area 3 – Municipal Capacity Building					
5. Annual Capacity Development Plans prepared by all LGs	Annual	LGs	Capacity Development Plans adopted by LGs and communicated to the CPSCL	DLI 6	[ ]
6. Preparation of standard terms of reference for feasibility studies of investments in disadvantaged neighborhoods	CY 14	CPSCL	Standard Terms of Reference approved and disseminated to LGs.		[ ]
7. Environment and social Manual (ESM) developed that provides updated procedures for environmental and social management for LGs to address gaps identified in the ESSA, including: (i) public consultations, public disclosure and grievance redress mechanisms; (ii) social assessment; (iii) land acquisition and resettlement procedures; (iv) screening of high-risk activities which are ineligible for Program support; and (v) monitoring and evaluation.	Effectiveness	CPSCL	Manual acceptable to the Bank has been approved		[ ]

8. Specific training modules consistent with the provisions of the POM have been developed and are made available to the LGs	CY 14	CFAD	Training modules included in the set offered to LGs		[ ]
9. Specific training modules on financial management for municipal financial management staff are developed and a national wide training program is initiated	CY 14	CFAD	Training module developed and nation-wide training program is planned and budgeted for		[ ]
Results Area 4. Country Systems Improvement					
10. A revised decree is adopted by the ANPE which addresses gaps identified in the ESSA, including (i) screening and categorization of activities requiring an EIA or an EMP; (ii) public consultations, public disclosure and grievance mechanisms; (iii) social assessment; and (iv) monitoring and evaluation.	CY 17	ANPE	The revised decree has been approved		[ ]
11. The capacity of the Court of Auditors and in particular its local branches is improved in order to perform annual financial audits of municipalities based on risk and in compliance with international norms of auditing (ISSAI).	Sep 30 of Program CY 16, 17, and 18	Court of Auditors	Annual audits of LGs are completed as per targets set in DLI 7 for CY 16, CY-17, and CY 18	DLI 8	[ ]
12. Municipalities to prepare and implement annual action plans to address audit findings within a period of six months after the receipt of the audit report.	March 30 of CY 17, 18, and 19.	LGs	Program Reports provided by CPSCL		[ ]
13. Citizen's Bureau in each municipality to be operationalized and their performance in grievance resolution monitored by the municipal councils.	CY 15	LGs and DGCPL	Program Reports provided by CPSCL		[ ]
14. Good Governance Cells established in all municipalities by the second year of the Program.	CY15	LGs and DGCPL	Program Reports provided by CPSCL		[ ]

Annex 9: Implementation Support Plan

1. The Implementation Support Plan (ISP) for the Program outlines the approach the Bank will take to support the Government's efforts to implement the Program activities and manage the key risks to achieving results and PDO.

2. Key focus areas: In addition to ensuring compliance with OP 9.00 and the Program's financing agreement, and based on the main conclusions of the preparatory assessments, the following areas have been identified as most critical to concentrate the Bank's implementation support efforts:

- **Introduction of the performance-based grant system:** While the Government and its agencies, particularly CPSCL have considerable experience in setting guidelines for municipalities and supporting them with municipal investment planning, financing and implementation, the performance-based grant instrument and assessment mechanisms of the Program will be a new function. The priority for strengthening within the CPSCL should be to institutionalize the capacity to manage the performance-based grant mechanism and, more broadly, the capacity of supporting agencies including DGCPL, CFAD and CPSCL to assist the municipalities to improve the governance, the sustainability and management of their municipal actions and services using clearly defined, measurable, and achievable results as a reference framework. The PA manual will serve as the guidelines for the Program and a key reference and guide for the municipalities. The Bank's support for the development of the PAM will be a key area of technical assistance.
- **Environmental management and monitoring capacity at municipal level:** Environmental risk is considered to be moderate given the small scale of the infrastructure and limited environmental impact during the construction and operational phases of the sub-projects. However, a capacity building program will be necessary for the implementing agencies to focus on procedures for document preparation and implementation. Strengthening the capacity to monitor and evaluate environmental performance indicators and to improve public consultation is also needed.
- **Limited fiduciary capacity in participating cities:** The Task Team will need to work with the CPSCL to ensure that municipalities have capable procurement staff and receive necessary procurement training. The Fiduciary Systems Assessment identified specific measures to improve the fiduciary performance of the Program, and these have been included in the Program Action Plan.

3. During the first year of implementation, the Bank's support will focus on strengthening the Program systems, especially the CPSCL's ability to support municipalities with their governance, sustainability and management performance as they prepare infrastructure sub-projects and the institutional activities necessary to achieve the DLIs. The Bank will also support: (i) the DGCPL with the design and the implementation of the proposed e-portal on local government performance; (ii) the CGSP - the public entity in charge of the performance assessments - in designing and preparing the LG performance assessment system; and (iii) CFAD in preparing a simple manual to guide LGs in their participatory municipal investment planning process. It is anticipated that the first year will require significant implementation support from the Task Team and selected international and local experts.

Table 1: Main focus of Implementation Support

Time	Focus	Skills Needed	Resource Estimate	Partner Role
First twelve months	• Strengthening of Program environmental, social, and fiduciary systems • Building CPSCL capacity to manage a performance-based grant mechanism • Support for local level institutional improvements • E-portal and access to information initiatives • Monitoring and Evaluation	• Procurement and FM training • Resettlement training and awareness building • Performance-based grant systems expertise • M&E expertise • Participatory planning expert	$300,000 BB	
12-48 months	• Support CPSCL and CGSP in verification mandate • Monitoring of key Program systems	• Procurement and FM systems expertise • Environment and social systems expertise • Municipal finance, Engineering and Asset management expertise	$250,000 per year	

4. A decentralized implementation support model is proposed for this operation, and it is envisioned that members of the Task Team will be primarily based in the country office. This will facilitate selected monitoring of sub-project activities in the participating cities. Specialized expertise related to establishing an M&E system for the Program, implementing the performance-based grant system, and input on technical area will likely come from international staff or consultants. In addition, the Bank will hire an Independent Verification Agent (IVA) to support the verification of the achievement of the Disbursement Linked Results.

Table 2: Task Team Skills Mix Requirements for Implementation Support

Skills Needed	Number of Staff Weeks	Number of Trips	Comments
Fiduciary	8	3	Country office
Environmental	8	3	Country office
Social	8	3	International
M&E	8	2	International
Institutional development and capacity building	12	3	International
Performance-based grant	12	3	International