PROJECT INFORMATION DOCUMENT (PID)
CONCEPT STAGE

Report No.: PIDC825

<table>
<thead>
<tr>
<th>Project Name</th>
<th>TN-Urban Development (P130637)</th>
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<tbody>
<tr>
<td>Region</td>
<td>MIDDLE EAST AND NORTH AFRICA</td>
</tr>
<tr>
<td>Country</td>
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<td>Sector(s)</td>
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<td>Theme(s)</td>
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<td>Government of Tunisia</td>
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<td>Implementing Agency</td>
<td>XXX</td>
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<td>Date PID Prepared/Updated</td>
<td>22-Mar-2013</td>
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<td>01-May-2013</td>
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<td>Estimated Date of Appraisal Completion</td>
<td>28-Jun-2013</td>
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<td>Estimated Date of Board Approval</td>
<td>31-Oct-2013</td>
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<td>Concept Review Decision</td>
<td>Track II - The review did authorize the preparation to continue</td>
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I. Introduction and Context

Country Context

1. Tunisia is currently going through a transitional phase of democratic and political reform. This process began in January 2011, when popular protests ended over two decades of President Ben Ali’s rule. The January 2011 revolution was largely driven by widespread dissatisfaction with a lack of socio-political inclusion, numerous governance issues, serious economic problems – such as rising unemployment – and by mounting frustrations with ever-widening social disparities.

2. The Constituent Assembly (CA), elected in October 2011 by ninety percent of the 4.1 million registered voters, is now in the process of drafting a new Constitution. The draft Constitution is expected to be ready by July 2013. Once the new Constitution is adopted, there will be a fresh round of national elections, currently expected to take place at the earliest in October.
2013. However, given the fluidity of Tunisia’s political transition, these timelines will need to be closely monitored and may well be subject to adjustment.

3. Recent drafts of the new Constitution include clear commitments to decentralization and to empowered local governments. The draft enshrines key principles: (a) the administrative autonomy of local governments (“libre administration des collectivités locales”); (b) subsidiarity (“subsidiarité”), i.e. the principle that matters should be administered at the lowest tier where they can effectively be managed; and (c) any transfer of competence from the State to a lower tier should be accompanied by the transfer of matching resources. The draft includes provisions for up to three tiers of directly or indirectly elected local governments to cover the entire country, ex-post (rather than ex ante) central oversight, and for full citizen participation in local development. These constitutional principles and provisions are to be translated into a fundamental law (“loi organique des collectivités territoriales”)

Sectoral and Institutional Context

4. Tunisia is one of the most highly urbanized countries in the Middle East and North Africa. In 1975, the country’s rate of urbanization was already 50%; today, roughly 70% of the country’s 10 million citizens live in towns and cities, most of them in the coastal Mediterranean belt. As in other countries, Tunisia’s urban sector is the most vibrant part of the national economy, accounting for more than 85% of GDP.

5. Economic growth has been concentrated in Tunisia’s coastal strip. This has resulted in persistent inequalities between coastal and inner regions, fuelling perceptions of territorial injustice and social exclusion. Inter-regional or inter-urban inequalities do not appear to be properly addressed through public investments: the poorer regions and towns of the interior have not benefitted from significantly higher public investments (per capita) than the more affluent coastal strip. Although data are not sufficiently disaggregated to provide statistical evidence of intra-urban disparities, there is much anecdotal evidence to indicate that municipalities include both poor and affluent neighborhoods, with significant variations in the quality of basic municipal services.

6. If Tunisian municipalities are very different in terms of size, they all share – to varying degrees – some common attributes: they have few responsibilities, play a relatively minor role in urban/local development, and enjoy limited decision-making powers. That communal budgets, in total, account for only 4% of total public expenditure is indicative of the relatively minor role played by municipalities in the Tunisian public sector as a whole.

7. Under “normal” circumstances, Tunisian municipalities are governed by a council, directly elected for a 5-year mandate, and an executive headed by the mayor, elected from among the councilors (except Tunis, where the mayor is named by decree from 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, not scheduled for the moment.

8. Elected municipal councils and mayors, however, were always subject to administrative supervision (or “tutelle”), whereby key commune 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 in practice.
9. Historically, and in the shadow of first a colonial and then a centralized patrimonial state, Tunisian communes 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. Current weaknesses in levels of citizen participation and accountability of the local government system can be partly attributed to constrained communal responsibilities, the absence of incentives for municipalities to facilitate citizen engagement, and to a traditionally centralized and authoritarian political regime. However, 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. By law, municipalities 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 municipalities. 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 political changes, greater local capacities, infrastructure maintenance requirements, and the need to sustain and improve the quality of services.

11. At the national level, municipalities are regulated and monitored by the DGCPL, a key directorate within the Ministry of the Interior. In addition to its regulatory functions, the DGCPL is also responsible for management of the FCCL (Fonds Commun des Collectivités Locales, or Local Government Common Fund – see below), which provides communes with annual block grants. The CPSCL (see more below), which is primarily accountable to the Ministry of Interior and the Ministry of Finance, provides communes with access to credit as well as to central government funding in order to finance municipal investments.

12. Municipal expenditures are dominated by spending on two sectors: municipal solid waste collection and street networks (construction and maintenance) together account for approximately 80% of total municipal expenditures (recurrent and capital). Communal 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 règle”), resulting in inflated payroll commitments while at the same time under-spending on other operations & maintenance tasks. For instance, the DGCPL estimates that up to 70% of communal 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.

13. Despite recent reforms, local government own-source revenues derive from a relatively weak and largely pre-determined base. Since 2011, the situation has deteriorated: low rates of tax collection have resulted in a decline in own-source revenues of roughly 40%, leaving many (if not most) municipalities unable to meet their payroll commitments. In 2011, total own-source revenues (taxes, charges, fees, etc.) represented less than 50% of total local government revenues (OSRs, fiscal transfers, etc.). The situation in 2012 is projected to be much the same, despite the
Government’s recent efforts to boost locally-levied business taxes. As a result, most post-2011 municipalities have become increasingly reliant upon fiscal transfers from the central government.

14. As in all inter-governmental fiscal systems, Tunisia’s has always included an important center-to-local transfer component. The clearest and most transparent element of this inter-governmental fiscal transfer (IGFT) system has been the FCCL, the volume of which is decided upon every year, and then allocated to all communes on the basis of a formula. The FCCL is managed by the DGCPL. FCCL allocations to communes 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%) has been growing in recent years, increasing from around US$103 million in 2008 to a little over US$160 million in 2012.

15. In less predictable and transparent ways, the central government also provides municipalities with capital budget “transfers” in the form of investment-by-investment “subsidies”. These “subsidies” are usually linked to municipal borrowing from the CPSCL and to the 5-year investment planning process (the PIC, currently for the period 2010-14), through which communes 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 “subsidies” are provided). Central government subsidies (effectively “hidden” inter-governmental fiscal transfers) thus account for about a third of commune investment expenditures.

16. As mentioned above, municipalities finance a proportion of their annual investment budget through borrowing from CPSCL. In principle, credit and “subsidies” for municipal investments are fairly rigidly linked together through PIC financing arrangements. Over time, this has led to high levels of municipal debt. By mid-2005, outstanding municipal debt was 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 communes. Despite debt-restructuring plans and other measures, the situation today remains much the same.

Recent orientations

17. In the aftermath of the “Jasmine Revolution” of 2011, Tunisia’s interim political authorities have had to seriously rethink the role of the State, question the added value of a high level of centralization, and revisit the role and importance of municipalities in urban development. Most importantly, the Constituent Assembly has now put forward an initial draft of the new constitution which enshrines (see section 6) the basic principles of decentralization, and increases the autonomy and authority of local government, largely by scaling back the central government’s oversight – or tutelle – powers and functions. The new constitution, once promulgated, will mark a fairly significant change in the relationship between central and local government.
18. The Interim Government has also signaled its intent to bring municipalities/cities into the heart of the urban development process – by making them more active players in the planning, implementation and delivery of municipal infrastructure and services. Among senior government officials there is a widespread recognition that elected municipal councils and mayors must be more than “passive spectators” in urban development. Moreover, there is a general consensus that, if they are to play a greater role, communes need to become more transparent and accountable to local citizens. There is also a high degree of unanimity that local government can only “deliver the goods” effectively if it operates within a more conducive fiscal/financial framework, one which provides communes with predictable fiscal transfers on a transparent and equitable basis and which also provides real incentives for communes to improve their performance. Finally, key central government departments (such as CPSCL and DGCPL) recognize the need to reform and reorganize the way in which capacity building support is provided to local governments.

19. Finally, for the period 2014-18, the Government has drawn up a program of financial support to assist local governments in the implementation of their municipal investment plans and to address intra- and inter-regional socio-economic disparities. In total, this Government program is costed at approximately US$ 770 million. In order to implement this program, the Government has requested the Bank to provide support.

Relationship to CAS

20. The project concept is consistent with the Bank’s Interim Strategy Note (ISN) for 2013-14.

21. The proposed project is fully aligned with the ISN’s second area of engagement: promoting social and economic inclusion. Within this second area, the project addresses driving objective 5, improving access to basic services for under-served communities. The project aims to lead to tangible and sustainable improvements in local level infrastructure and service delivery by: (i) financing a more equitable flow of performance-based fiscal transfers to municipalities; (ii) improving municipal performance and governance; and (iii) strengthening municipal capacities.

22. The proposed project is also generally in line with the ISN’s third area of engagement: strengthening governance through voice, transparency and accountability. The project’s focus on local governance institutions, in particular, and decentralization, in general, is linked to making communes more accountable and more open to citizen voice and participation.

23. Finally, the project resonates with the Bank’s overall framework for engagement in the MENA region. The project seeks to: (i) strengthen governance, in general, and local governance, in particular, by enhancing the functions, financing and capacities of local governments; and (ii) increase the inclusiveness of local service delivery in Tunisia by providing municipalities with the resources to finance the upgrading of informal and disadvantaged neighborhoods, particularly in lagging regions. As such, the project directly addresses two of the four main pillars in the Bank’s regional framework for engagement.

II. Proposed Development Objective(s)

Key Results (From PCN)

34. Four results will be delivered by the project:
(i) Access to and quality of key municipal services improved;

(ii) Infrastructure and services in informal neighborhoods (“quartiers populaires”) upgraded;

(iii) Participatory and accountable planning processes for municipal infrastructure introduced; and

(iv) Access to information about municipal investment plans, budgets and expenditures promoted.

III. Preliminary Description

Concept Description

29. The proposed Urban Development and Local Governance Project (UDLGP) will be structured around the following components:

Component 1: Institutional support and capacity development

Sub-Component 1-1: Decentralization and local governance

30. During the lifetime of the proposed project, the Government will be engaged in fleshing out constitutional reforms, one of which will be linked to deepening and strengthening decentralization and local governance processes. To complement and enhance these processes, the project will provide the following institutional support:

(i) Technical assistance for formulating an appropriate and revitalized legal framework for local government in Tunisia, building on new constitutional provisions. This will include an organic law on local government, legislation on fiscal decentralization, and a range of associated implementation regulations. International technical assistance will ensure that Tunisia profits from established good practice in other countries; national technical assistance will enable the Government to tailor international good practice to the specificities of the local context.

(ii) Technical assistance for establishing a thoroughgoing system through which citizens are regularly informed of local government decisions, budgets, expenditures and service delivery. This will be based on: (a) legal provisions (and enforcement of those provisions) for local governments to publicly disclose such information; and (b) a centrally-managed system that provides such information to citizens on a regular basis.

(iii) Technical assistance for developing ICT-based interfaces for municipal services (such as vital registration, waste collection, etc.) so as to enhance accountability and improve grievance redress mechanisms.

(iv) Technical assistance for developing and establishing up-graded municipal accounting software.

Sub-Component 1-2: Municipal capacity development
31. This sub-component will operate at sub-national levels and will provide support in a number of areas:

(i) Reviewing and revising the current municipal investment planning process, to make it more participatory, actively engage communes throughout the process by turning them into the principal anchors for the identification, prioritization and implementation of investments. This is likely to be incremental, and will require not only a change in the approach taken by municipalities, but also changes in CPSCL modalities and the way in which municipalities access funding from the central government.

(ii) Developing tools, guidelines and training materials to strengthen municipal operations and maintenance (O&M), which have been a neglected dimension of local service delivery. This will entail the introduction of asset inventories, regular maintenance planning, and better supervision/monitoring methods. The primary focus will be on O&M for waste collection and for street/pavement maintenance.

(iii) Provision of demand-driven capacity building support for core municipal functions (e.g. planning, financial management, maintenance, asset management, etc.). This will be complementary to the capacity development services obtained by municipalities through the capacity building block grants.

(iv) Expanding the scope of GIS-based management tools and increasing the number of communes using GIS-based applications.

Component 2: Municipal investments and finance

Sub-Component 2-1: Performance-based municipal block grants and more coherent investment financing

Financing municipal investments. Under the project, central government subsidies to local government investments will be gradually consolidated into annual, general purpose, development grants. While the overall funding pool made available by the central government to local governments will remain more or less at current (inflation-adjusted) levels, financing modalities (“schemas de financement”) will be modified so as to gradually move towards a system whereby central government budgetary subsidies for municipal investments effectively take the form of annual capital block grants. Each commune will have access to a full “drawing right”, calculated on the basis of a simple and transparent formula (in much the same way as recurrent budget allocations are made to communes from the FCCL). Full “drawing rights” for each commune will be calculated on the basis of a simple formula that will include criteria such as municipal population size and the relative poverty of each commune (in order to take into account inter-regional disparities).

Performance-based municipal block grants. Through the project, the annual block grants allocated to municipalities from the FCCL will be divided into two parts:

(i) Basic Block Grant (BBG)

Defined as a proportion of their total “drawing right”, the BBG will be made available to communes on the basis of their compliance with a set of minimum conditions (MCs). MCs would consist of
statutory (or legislative) requirements, as spelled out in the Local Government Code and other pieces of legislation. Full compliance with MCs would allow communes to access their full BBG allocations.

(ii) Performance-Based Grant (PBG)

The remainder of each commune’s “drawing right” would consist of a PBG. Municipalities would access their PBG allocations on the basis of their prior performance, assessed on an annual basis and measured with respect to a range of performance areas (e.g. infrastructure and service delivery, financial management, fiscal effort, transparency and accountability, etc.). Communes will be scored on the basis of their performance and allocated a proportion of their PBG allocation. As a consequence, the highest scoring communes would access the entirety of their PBG allocation, while lower scoring communes would access proportionately less.

Detailed BBG and PBG modalities (proportion of “drawing rights”, indicators, etc.) will be discussed and decided on during project preparation, based on agreed principles, good international practice, and on-the-ground realities and context.

BBGs and PBGs will provide communes with tangible fiscal incentives to: (i) ensure compliance with legal provisions for local government; and (ii) improve their performance over time. The CPSCL/DGCPL would out-source and oversee the annual performance assessment process. Importantly, assessments will only focus on those aspects of performance that can be directly attributed to communes, and for which local governments are wholly responsible. Assessment outcomes and their implications for budget allocations, once endorsed by an Inter-Ministerial Committee, would be publicly disclosed by the CPSCL/DGCPL, thus allowing local citizens to become aware of the performance of their municipalities.

This performance-based grant system will build upon existing features of and arrangements for municipal allocations from the FCCL, and will be introduced in an incremental way. Communes will be taken up gradually, so that by the end of the project all municipalities will have been “enrolled” into the new system of FCCL grants.

Sub-Component 2-2: Municipal investments targeted at reducing unequal access to public goods and services with a focus on lagging regions/cities.

The project will also include a financing facility that will provide municipalities with access to earmarked grants for improving access to basic municipal services i.e. upgrading informal neighborhoods (“quartiers populaires”). In contrast to previous informal neighborhood upgrading programs, this will be (as far as possible) demand-driven and target lagging regions and cities. The Government will establish a funding facility which will be jointly managed by the CPSCL and the Ministry of Regional Development and Planning. Selected municipalities will be able to obtain financial support from this facility to undertake investments aimed at providing residents in informal neighborhoods with basic municipal goods and services (streets, lighting, drainage, etc.).

IV. Safeguard Policies that might apply

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Page 8 of 10
V. Financing (in USD Million)

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Total Project Cost: 100.00
Total Bank Financing: 100.00
Financing Gap: 0.00

VI. Contact point

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