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PERFORMANCE AUDIT REPORT

INDONESIA

**EAST JAVA/BALI URBAN DEVELOPMENT PROJECT
(LOAN 3304-IND)**

**SULAWESI/IRIAN JAYA
MUNICIPAL/URBAN DEVELOPMENT PROJECT
(LOAN 3340-IND)**

June 22, 2001

*Sector and Thematic Evaluation Group
Operations Evaluation Department*

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Currency Equivalents

Currency Unit = Indonesian Rupiah (Rp)

(as of January 1991)

Rp 1 million = \$526; \$1.00 = Rp 1,901

(As of September 1997)

Rp 1 million = \$305; \$1.00 = Rp 3,275

Abbreviations and Acronyms

CAS	Country Assistance Strategy
EASUR	East Asia and Pacific Region Urban Development Sector Unit
EJB UDP	East Java/Bali Urban Development Project (Loan 3304-IND)
GOI	Government of Indonesia
ICR	Implementation Completion Report
IUIDP	Integrated Urban Infrastructure Development Program
KIP	<i>Kampung</i> (neighborhood) Improvement Program
LIDAP	Local Institutional Development Action Plan
MIIP	Market Infrastructure Improvement Program
O&M	Operations and Maintenance
OED	Operations Evaluation Department
PAR	Performance Audit Report
PDAM	Local Water Enterprise
PFAMS	Project Financial Accounting and Management System
PJM	Medium term (5-year) plan for infrastructure and finance
POMMS	Performance Oriented Maintenance Management System
REPELITA	Five-Year Development Plan
RIAP	Revenue Improvement Action Plan
SAR	Staff Appraisal Report
SIJ UDP	Sulawesi/Irian Jaya Urban Development Project (Loan 3340-IND)
SLAP	Subsidiary Loan Agreements with Pre-Financing
SPABP	Funds Channeling Documents for Special Grants to Lower Level Governments

Fiscal Year: Government of Indonesia: April 1 - March 31

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Office of the Director-General
Operations Evaluation

June 14, 2001

MEMORANDUM TO THE EXECUTIVE DIRECTORS AND THE PRESIDENT

**SUBJECT: Performance Audit Report on Indonesia
East Java Bali Urban Development Project (Loan 3304-IND)
Sulawesi Irian Jaya Urban Development Project
(Loan 3340-IND)**

This is a Performance Audit Report (PAR) on the Indonesia East Java/Bali Urban Development Project (EJB UDP) and the Sulawesi/Irian Jaya Urban Development Project (SIJ UDP) (Loans 3304-IND and 3340-IND). The EJB UDP was approved on March 19, 1991, for \$180.3 million, and it closed on September 30, 1997, nine months after the original closing date, canceling \$7.3 million. The SIJ UDP was approved on June 6, 1991, for \$100.0 million and it closed on June 30, 1997, six months after the original closing date (\$4.2 million was transferred from the currency pool to a fund for emergency poverty relief to alleviate the impacts of the financial crisis). Final disbursement of the EJB loan took place on February 9, 1998, and on November 25, 1997, for SIJ.

Within the framework of the Integrated Urban Infrastructure Development Program (IUIDP) the GOI pursued an integrated approach for preparing and implementing local urban improvement programs. IUIDP was the centerpiece of national decentralization efforts. The approach was to encourage local governments to plan and fund their own projects and generate their own revenues, a major departure from earlier efforts.

The EJB and SIJ UDPs were the first two major projects in the IUIDP series financed by the World Bank. The IUIDP approach was subsequently adopted by over 75 percent of the local governments, and became the basis for donor-supported urban programs throughout Indonesia—more than 20 urban projects have been financed under the IUIDP approach. The two projects' basic objectives were to improve urban infrastructure; increase access of households to water supply and sanitation services; support local government capacity for operations and maintenance (O&M); improve financial management (including expenditure programming, financial planning and information management); and to strengthen local government institutions and human resources. To meet these objectives, the projects consisted of several key components: infrastructure development; infrastructure rehabilitation; operations and maintenance; technical assistance for project implementation and local management; and institutional capacity building.

Preparing nine large and complex IUIDPs that would all be initiated within a three-year period led to an agreement on general principles, but little attention to the details of participating cities (particularly those that had a lower capacity for planning on their own). Although project implementation was more challenging in large metropolitan areas because of their complexity, in the smaller cities a lack

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of institutional capacity to execute the project was often encountered. The regional economic crisis of 1997 changed the environment in which the cities were operating, constraining resource flows, making these already difficult projects more so.

The audit supports the two ICRs' accounts of project experience, including their criticism of insufficient institutional development, ad hoc sectoral master planning, and failure to advance the urban agenda. It also finds that Bank-financed O&M in the two evaluated projects was notably ineffective. (On the other hand, this is a common problem facing infrastructure investments in Indonesia.) The audit notes additional instances of unmet targets and identifies several examples of unintended negative environmental impacts.

The audit rates project outcome for EJB as moderately satisfactory, sustainability as unlikely, and institutional development impact as modest. This differs from the ICR, which rated overall outcome of the project as satisfactory. Although the project achieved most of its physical objectives and relevance was high, there were significant shortcomings including costly errors due to a lack of supervision, and infrastructure lying in disuse or, worse, built twice. The audit rates SIJ project outcome as moderately satisfactory, sustainability as unlikely, and institutional development impact as modest. These ratings are essentially equivalent to those of the ICR. Although the project achieved most of its physical objectives efficiently, there were significant shortcomings—infrastructure had seriously deteriorated, maintenance was not being performed, and institutional weaknesses persist. While official enthusiasm for an integrated approach to development is high, and most of the physical infrastructure for the two projects was successfully built, the resiliency of project benefit flows to risk (and economic crisis) is low because attention to routine maintenance and service sequencing was lacking (allowing uncollected refuse to block storm sewerage, for example). Another factor that lowered the projects' sustainability rating was sub-optimal institutional progress.

Expectations that municipal practices would change rapidly were unrealistic. External events are highlighting the importance of the integrated planning concepts nevertheless. Economic crises have at least one positive impact: they provide enormous incentives for better financial management, and they penalize the tendency to (expensively) focus on short-term needs on an ad hoc basis. Lessons identified include the importance of identifying the minimum necessary conditions for success, providing incentives for planning updates, and giving uninterrupted attention to the environment lest damaging activities escape the requisite scrutiny.

Attachment

A handwritten signature in black ink, consisting of a large, stylized 'S' or 'C' shape followed by a series of loops and a final vertical stroke.

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This report was prepared by Ronald Parker and Kristin Little, who audited the project in June 2000. William Hurlbut edited, and Helen Phillip provided administrative support.

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Principal Ratings

	<i>Outcome</i>	<i>Sustainability</i>	<i>Institutional Development</i>	<i>Borrower Performance</i>	<i>Bank Performance</i>
East Java/Bali Project (Loan 3304)					
Implementation Completion Report	Satisfactory	Uncertain	Partial	Satisfactory	Satisfactory
Audit	Moderately Satisfactory	Unlikely	Modest	Satisfactory	Satisfactory
Sulawesi/Irian Jaya Project (Loan 3340)					
Implementation Completion Report	Marginally Satisfactory	Unlikely	Partial	Satisfactory	Marginally Satisfactory
Audit	Moderately Satisfactory	Unlikely	Modest	Satisfactory	Satisfactory

Permitted Ratings

<i>Outcome</i>	Highly Satisfactory, Satisfactory, Moderately Satisfactory, Moderately Unsatisfactory, Unsatisfactory, Highly Unsatisfactory
<i>Sustainability</i>	Highly Likely, Likely, Unlikely, Highly Unlikely, Not Evaluable
<i>Institutional Development Impact</i>	High, Substantial, Modest, Negligible
<i>Bank Performance</i>	Highly Satisfactory, Satisfactory, Unsatisfactory, Highly Unsatisfactory
<i>Borrower Performance</i>	Highly Satisfactory, Satisfactory, Unsatisfactory, Highly Unsatisfactory

Key Staff Responsible

	<i>Task Manager</i>	<i>Division Chief</i>	<i>Country Director</i>
East Java Urban Bali Urban Development Project (Loan 3304-IND)			
Appraisal	Ben Fisher	Lars Jeurling	Russell Cheetham
Interim	Steve Dice	Anupam Khana	Marianne Haug
Completion	Raja Iyer	Keshav Varma	Dennis de Tray
Sulawesi/Irian Jaya Project (Loan 3340)			
Appraisal	Lazlo Lovei	Lars Jeurling	Russell Cheetham
Interim	Heinrich Unger	Anupam Khana	Marianne Haug
Completion	Dan Hoonweg	Keshav Varma	Dennis de Tray

Preface

This is a Performance Audit Report (PAR) on the Indonesia East Java/Bali Urban Development Project (EJB UDP) and the Sulawesi/Irian Jaya Urban Development Project (SIJ UDP) (Loans 3304-IND and 3340-IND). The EJB UDP was approved on March 19, 1991, for \$180.3 million, and it closed on September 30, 1997, nine months after the original closing date, canceling \$7.3 million. The SIJ UDP was approved on June 6, 1991, for \$100.0 million and it closed on June 30, 1997, six months after the original closing date. (US\$4.2 million was transferred from the currency pool to a fund for emergency poverty relief to alleviate the impacts of the financial crisis.) Final disbursement of the EJB loan took place on February 9, 1998, and on November 25, 1997, for SIJ.

This Operations Evaluation Department (OED) report for the two projects is based on the Staff Appraisal Reports, President's Reports, sector and economic reports, special studies, Country Assistance Strategy, loan documents, review of the project files, and discussions with Bank and Borrower staff. The Implementation Completion Reports for the SIJ and EJB UDPs¹ were prepared by the Urban Development Sector and the Indonesia Country Management Units of the East Asia and Pacific Region. An OED mission visited Indonesia in July of 2000 and discussed the effectiveness of the Bank's assistance with national, provincial, and local government officials, development organizations, and other stakeholders. Their kind cooperation and invaluable assistance in the preparation of this report are gratefully acknowledged.

The Implementation Completion Reports (ICRs) provide an account of the project experience and achievements. They cover project design issues and the relationship of the Bank with the borrower. The PAR discusses a number of problems that constrained the achievement of project objectives, and identifies a few new lessons learned. It assesses the quality of the intervention design, including its consistency with the problems identified. It reflects on the borrower's ownership and commitment; and determines the effectiveness of the project subcomponents.

This audit was recommended because these projects are a key link in the joint Government of Indonesia/World Bank effort to promote decentralization in the urban sector. The audit focuses on the appropriateness of the project design given the prevailing local conditions. The implementation experience was reviewed with special attention given to the projects' institutional capacity building achievements.

Copies of the draft PAR were sent to the relevant government officials and agencies concerned, for their review and their comments are attached.

1. SIJ: ICR, Report No. 17253, dated 12/22/97; EJB: ICR, Report No. 17529, dated 3/25/98.

1. Background

Country Context²

1.1 Prior to the mid-1970s, the Government of Indonesia (GOI) centrally planned and implemented all public works for this large archipelago. This approach became more and more impractical as the population swelled from 119 million in 1971 to over 147 million by 1980 (by 2001 it had grown to over 207 million), and cities grew at a rate of over 5 percent per year. In response to this pressing situation, the GOI adopted Law Number Five, which provided regional autonomy, laying the groundwork for decentralizing responsibilities. Following the severe economic decline in the mid-1980s, there was strong macroeconomic pressure to decentralize government operations. By 1991, only 40 percent of urban households had access to adequate sanitation facilities, 20 percent had direct access to piped water supply, and a substantial backlog prevailed in facilities maintenance, resulting in the decreased productivity of an already inadequate infrastructure.³

Role of the Bank

1.2 During the past two decades, the Bank has provided critical support and strategic input to the evolving urban policy agenda in Indonesia. By the time of project preparation, the Bank had financed 13 completed and 8 ongoing urban and water supply projects. It has supported the work of more than 60 local governments and helped them to invest in many of their water enterprises.⁴ In response to the crisis of the mid-1980s, the GOI articulated its priorities for the urban sector in a Statement of Policies for Urban Management issued in 1987 and incorporated these policies in the fifth national five-year plan,⁵ for the period 1989–94. Within this, the Integrated Urban Infrastructure Development Program (IUIDP) was the operational approach used to achieve the objectives of the Policy Statement. The centerpiece of decentralization, it served to encourage local governments to begin to plan and fund their own projects. The Statement, including IUIDP, became a joint approach of GOI and the Bank to address urban development in the country. The Bank's 1995 Country Assistance Strategy (CAS) for Indonesia highlights the need for improved public service delivery, greater decentralization of responsibilities, and improved environmental management.

1.3 The IUIDP approach was a major departure from earlier sectoral approaches. It recognized that urban management was necessarily multi-sectoral and complex, and attempted to get urban managers to prepare plans⁶ for urban infrastructure sectors by allocating the available limited resources optimally between sectors. At its inception in 1991, the East Java/Bali Urban Development Project (EJB UDP) was the flagship project under the IUIDP concept and the

2. See also discussion in: Operations Evaluation Department. *Indonesia Impact Evaluation Report, Enhancing the Quality of Life in Urban Indonesia: The Legacy of the Kampung Improvement Program*. (Washington, D.C.: The World Bank, June 29, 1995).

3. EASUR notes that this section of the PAR provides inadequate description of the strategic context of these projects and the paradigm shift they represent. Regional staff note that a fuller discussion of the “big picture” of the context would show that the “leadership or experimentation involved in negotiating the decentralization process for nearly every detail of these projects were a key feature of preparation and implementation of these projects.”

4. Referred to in project documents as PDAMs.

5. Repelita V.

6. PJMs.

Sulawesi/Irian Jaya Urban Development Project (SIJ UDP),⁷ followed just months later. The IUIDP approach was subsequently adopted by over 75 percent of the local governments, and became the basis for donor supported urban programs throughout Indonesia. To date, over 20 urban projects have been financed under the IUIDP approach, of which the Asian Development Bank financed 12, and the IBRD financed 8. Other donors have financed sub-components of some of these projects. Deficiencies found in early projects warrant serious attention because of the scale of ongoing projects⁸ and the long-term decentralization objectives of the GOI.⁹

The Urban Development Projects

1.4 The two Bank projects examined in this audit supported the IUIDP concept and the enhanced coordination of planning, implementation, and supervision among all levels of government, in order to improve the delivery of urban services and enable local governments to assume greater responsibility for urban management. Following the GOI policy of regionally balanced development,¹⁰ there was an attempt to spread funding for these projects widely across the country, despite regional variances in institutional capacity.¹¹

1.5 The EJB and SIJ UDPs were the first two major projects in the IUIDP series financed by the World Bank. The projects had similar objectives, were made up of many parts, and were implemented during roughly the same time period, 1991–98 (see table below). The two projects can be viewed as first efforts in a task that requires a series of sustained interventions to bring about long-term changes in government practice. Because of the importance of the IUIDP concept, the two completed projects have been clustered in one report so that any observed patterns that are common to both projects can be highlighted.

<i>name:</i>	EAST JAVA/BALI	SULAWESI/IRIAN JAYA
<i>loan no:</i>	Loan 3304-IND	Loan 3340-IND
<i>total cost:</i>	\$180.3 million, but cancelled \$7.3 million at closing	\$100.0 million
<i>approved:</i>	March 19, 1991	June 6, 1991
<i>closed:</i>	September 30, 1997 (Nine months after the original closing date)	June 30, 1997 (Six months after the original closing date)
<i>disbursement record:</i>	Final disbursement took place on February 9, 1998	Final disbursement took place on November 25, 1997

1.6 The fundamental objective of the two projects was to improve the quality of urban infrastructure investment and service delivery. The two projects' more detailed operational objectives were to:

7. Commonly known within the Bank and the implementing agencies as "SulIriJa."

8. Ongoing IUIDPs accounted for \$717 million in lending (\$198.8 cancelled) as of Oct 31, 2000. http://eap.worldbank.org/indonesia/bank_operations/Ongoing1.xls, consulted May 3, 2001.

9. EASUR wishes the audit to note that "detailed 'technical memoranda' covering each subsector, as well as planning processes, financial management, revenue enhancement, O&M and many other procedures were prepared for EJBUDP and adapted for the subsequent projects case-by-case. The underlying rationale for these projects was the support of GOI decentralization initiatives from the Urban Policy Action Plan, and this was substantially achieved by both projects."

10. As expressed in Repelita V.

11. This issue is described further in the Staff Appraisal Reports (EJB, p 15 and SIJ, p 14).

- a) **provide urban infrastructure** in selected cities with emphasis on increased access of households to water supply and sanitation services;
- b) **improve local level urban infrastructure expenditure programming, financial planning, and information management**; support the development of local government capacity to prepare and execute annual O&M programs; encourage local revenue generation, improve financial management, and strengthen local government human resources and institutions; and
- (c) **assist sector development nationwide**, including preparation of future projects.

1.7 To meet these objectives, the projects consisted of several key components (note where the two projects did not overlap), covering similar activities in different categories:

<i>name:</i>	EAST JAVA/BALI		SULAWESI/IRIAN JAYA	
	<i>\$ million budgeted</i>	<i>% of total project cost</i>	<i>\$ million budgeted</i>	<i>% of total project cost</i>
<i>infrastructure dev't/ rehabilitation :</i>	340.2	94.4%	146.3	86.6%
<i>technical assistance:</i>			22.7	13.4%
<i>program management:</i>	13.4	4.0%		
<i>institutional development:</i>	3.4	1.0%		
<i>sector development:</i>	3.5	3.5%		

1.8 The investments, in order of magnitude, included roads, operations and maintenance (O&M) for existing facilities and services, water supply, drainage, KIP (*Kampung* Improvement Program), solid waste management, sanitation/sewerage, and MIIP (Market Infrastructure Improvement Program). Components introduced in projects included: LIDAP (Local Institutional Development Action Plan), PFAMS (Project Financial Accounting and Management System), PJMs (medium-term plans), POMMS (Performance Oriented Maintenance Management System), RIAP (Revenue Improvement Action Plans), SLAP (Subsidiary Loan Agreements with Pre-financing), SPABP (Funds Channeling Documents for Special Grants to Lower Level Governments), environmental management, and local government financial accounting and management.

East Java/Bali UDP: The Flagship

1.9 With its tradition of administrative competence and its diversity of local conditions, East Java has been the site of Bank-funded urban projects for about 20 years.¹² With respect to resources, both human and financial, Java and Bali are considered the most “developed” of Indonesia’s islands.¹³ As such, they have benefited from much investment attention. Government representatives in East Java and Bali, had already implemented several World Bank projects, including Urban I, II, III, and V, EJ Water I, and EJ Water II.

1.10 At its inception, GOI and the Bank regarded the integrated EJB UDP as the “new model” for urban infrastructure and local services delivery programs and it is considered a key link in the GOI/Bank joint effort to promote decentralization in the urban sector. It was the first and largest

12. Java is known to be the “political, geographic, and economic center,” of Indonesia. It has “the bulk of Indonesia’s industry and it received most of the foreign investment that poured into the country in the 1990s” (Peter Turner. *Indonesia*. [London: Lonely Planet Publications Pty. Ltd., 2000] 169).

13. See, for example, discussion in Peter Turner, *Indonesia* (London: Lonely Planet Publications Pty. Ltd., 2000) 169.

in a series of IUIDPs, and it represents a radical departure from previous urban operations. The project was designed to be implemented in three batches in order to capitalize on the lessons of experience. In EJB, the cities and project sites are relatively close together, one to the next, facilitating supervision by the management units. Because there were so many project sites, Bank supervision was handled on a sample basis.¹⁴

Sulawesi/Irian Jaya UDP

1.11 The SIJ UDP, like EJB, was conceived and designed at roughly the same time as nine other IUIDPs. At the outset, SIJ was intended to be two separate projects, the Sulawesi Urban Development Project and the Irian Jaya Water Supply Project. These two relatively small loans were combined for a total loan amount of \$100 million, covering 9 local governments in Sulawesi and 8 water enterprises in Irian Jaya—the smallest of the IUIDPs.¹⁵ Time pressures, staff skills deficits, and lack of institutional capacity precluded the development of an integrated project in Irian Jaya and it was left as a single-sector (water supply) component. Lack of financial capacity put Sulawesi and Irian Jaya at a disadvantage compared to East Java and Bali. To add to the difficulties, unmet demand for water service was high in Sulawesi and Irian Jaya, and financial constraints made delivery difficult.

1.12 Bank staff opinions were mixed as to the appropriateness of the IUIDP approach in such a context, but in response to strong GOI preferences, the project went ahead as planned. Project preparation documents point out that “In other less developed parts of the country such as East Indonesia, where local capacity is less developed, regular project lending is more appropriate and cost recovery is more difficult. [However,] the Bank strategy recognizes that regionally balanced development is a legitimate concern of GOI and development of urban areas in the Eastern part of the country is necessary to achieve that.”¹⁶

1.13 Balancing development regionally presented many challenges. The two islands, Sulawesi and Irian Jaya, are located several hours by plane from Jakarta and many of the project sites in Irian were difficult to reach, making close supervision difficult. Nonetheless, Bank staff visited all sites at least once a year. Several Bank staff pointed out that it is not easy to get senior consultants to work in Sulawesi and Irian Jaya. And according to the SIJ Implementation Completion Report (ICR), one of the critical factors affecting the SIJ project was “inexperienced contractors and supervision consultants who were reluctant to work in isolated communities particularly in Irian Jaya.”¹⁷

1.14 With respect to intervention type, Sulawesi provincial and local governments “were not ready for programmatic operation,” according to the Staff Appraisal Report (SAR). The capability of local governments to prepare second and third “batch” investments and provincial governments to appraise those investments was not satisfactory. Therefore a decision was made to redirect the preparation effort toward a one “batch” traditional project-type intervention.¹⁸ The SAR further notes that the large size of the project given the existing capacity “reflects GOI’s

14. EJB ICR, p 9, para 42.

15. The appraisal report states: “The two preparation efforts were merged by GOI in June 1987, with agreement from the Bank.” (SIJ SAR, p 15).

16. SIJ SAR, p 14, para 2.22.

17. SIJ ICR, p iii, para ix.

18. SIJ SAR, p 15-6, para 3.2.

intention to provide urban services to as many people as possible during the current five year planning period.”¹⁹

2. Implementation

2.1 Preparing nine large and complex IUIDPs that would all be initiated within a three-year period led to an agreement on general principles but little attention to the details of participating cities (particularly those that had a lower capacity for planning on their own).²⁰ Problems of scale were recognized by IUIDP specialists, who noted that, in general, project implementation was more complex in large metropolitan areas (e.g., Jabotabek) and easier in smaller cities. However, the smaller the city is, the greater the chance of encountering a lack of institutional capacity to execute the project. The size of the projects, combined with their complexity, made the implementation of such a new concept even more difficult. The regional economic crisis of 1997 changed the environment in which the cities were operating, constraining resource flows, making these already difficult projects more so.

ICR Findings

2.2 The main findings of the Implementation Completion Reports prepared following the closing of each loan are presented below.

East Java/Bali

2.3 The ICR for EJB concludes that the physical components of the project were largely constructed as designed and they had been reasonably well maintained subsequently.²¹ It notes that the project had created important institutional development incentives to induce local governments to accept decentralization. And decentralization had contributed to the strengthening of local government institutions and led to improved urban infrastructure programming, financial planning, and information management within local governments. Further evidence of institutional development cited by the ICR was the active participation of involved cities in the design of two follow-on projects. The EJB ICR also reports enhanced local revenue generation, which was producing economic benefits that matched appraisal expectations.

2.4 The ICR is critical of integrated planning achievements, noting that this objective was not fully met and that integrated planning exercises did not have the desired impact when they were attempted (especially at the lowest government levels). In addition, project participants are criticized as having paid inadequate attention to preparing sectoral master plans as the basis for investment programs: the cities’ tendency to focus on short-term needs on an ad hoc basis was not overcome. The ICR also notes that the project failed to advance the sectoral agenda, especially in the water sector, pointing out that efforts to improve the financial management of participating

19. SIJ SAR, p 16, para 3.3.

20. Although city-specific details were dealt with by producing the medium-term plans, a process which was supposed to include a stakeholder consultation.

21. The ICR was submitted on March 25, 1998.

water enterprises were only partially successful; but it was optimistic because these issues are being addressed under the follow-on projects.²²

Sulawesi/Trian Jaya

2.5 The ICR concludes that the project successfully provided urban physical infrastructure, pointing out that most of the civil works financed under the project were handed over to the local water enterprises by the original closing date and are now in operation. The ICR admits that the concept and scope of IUIDP were not clear to all government agencies participating in project implementation, however. In retrospect, it finds that the project's risk assumptions (with regard to institutional objectives and implementation arrangements) were overly optimistic: Targets for water connections, unaccounted-for-water reduction, and increased tariffs, although based on thorough feasibility studies, may have been higher than actually could be delivered with the available resources and institutional capacities of the local governments and their water companies. The ICR criticizes local procurement procedures, construction quality, the post-project percentage of unaccounted-for water, ineffective O&M, marginal economic rates of return (water, road, and drainage components), and a lack of sufficient involvement of some local governments in planning, design, and implementation. Furthermore, the ICR reports only partial compliance with loan covenants for operations and maintenance and tariff adjustments (to fully cover the real costs of water service).

2.6 With respect to institutional development, the ICR finds that the project suffered from a lack of local government capacity to prepare and execute O&M programs, infrastructure programming, and financial planning. Little progress was made in the institutionalization of the IUIDP concepts and follow-up mechanisms. Local capacity to deliver urban services was only marginally improved. Although municipal revenues increased and financial management improved, the ICR speculated that this was not a result of project efforts.

PAR Findings

2.7 The audit basically supports the two ICRs' accounts of project experience, including their criticism of insufficient institutional development, ad hoc sectoral master planning, and failure to advance the sectoral agenda, although it differs with the EJB ICR on targets met/unmet. It also finds that Bank-financed O&M in the two evaluated projects was notably ineffective. (On the other hand, this is a common problem facing infrastructure investments in the country.) The audit notes several instances of unintended negative environmental impacts and flags this issue as a shortcoming of these projects.

Progress and Problems with Integrated Planning

2.8 In general the audit mission encountered considerable central, provincial, and local government support for a more holistic approach to planning. One official had even independently taken the concept and begun applying it in villages, obtaining active participation by rural stakeholders. Though the SIJ ICR declares that "little progress was made in institutionalization of the IUIDP concepts and follow-up mechanisms," the audit mission found that, in both EJB and SIJ at least, significant attitudinal change was evident. In numerous discussions with local officials, the audit mission observed an awareness of the potential benefits

22. The observation comes from the EJB ICR, p v. In a written comment on this paragraph of the PAR, the GOI pointed out that efforts to improve the performance of the water enterprises take a long time, and they require a willingness to improve on the part of the target enterprises.

of integrated sectoral planning, especially on the part of Public Works officials. Before the projects, they dealt only with roads. Suddenly, in charge of the Project Management Unit, they had to consider the implications of project actions on all sectors and this may have permanently changed their way of thinking. Also promising are reports that the nine municipalities in Sulawesi II with previous IUIDP experience are performing much better than those without, according to Sulawesi II project managers.

2.9 Nonetheless, difficulties with integration abound. Planning was too often integrated on paper, but not followed in decision-making. In a memo on the results of SIJ (in a follow-on project preparation document found in the files) one involved Bank staff noted:

“Goal-setting is rarely in evidence; it is certainly not included in any systematic way in the preparation of [municipalities’ medium-term plans]. Only in master plans are strategies, goals, and targets enunciated at least in minimal fashion. Many sectors in many cities do not yet have master plans, and there is rarely an attempt to systematically identify priorities within sectors, let alone between sectors. IUIDP cannot be considered to be an urban planning approach until goal setting and prioritization are introduced as integral activities. To date the practice has been one of programming rather than planning.”

Medium-Term Plans (PJMs)

2.10 Included in both the EJB and SIJ projects was the concept of creating five-year, medium-term plans (PJMs) in each local government. Several problems resulted from this approach. First, the plans were often prepared in a hurry, usually by consultants (with the notable exception of Bali) so that local officials felt little ownership. There was little integration at the regional level, in part because consultants were selected and hired by central government agencies. The planning documents produced have tended to be identified by municipal employees and officials as central government products rather than the local governments’ own document.²³ The plans often contained faulty estimations of need. For example, when calculating water demand, consultants for the EJB project were reported to use the same parameters for dense and sparsely populated areas, thus throwing off the estimates. Or, they would consider dwelling numbers apart from occupation rates.

2.11 The consultants helping local governments to prepare these plans were supposed to transfer their knowledge. In reality, they found few relevant skills and even less interest on the part of the local government and, under severe deadline pressure, the consultants put together the plans without meaningful participation from the local government.²⁴ This created several problems. The consultants were not local and thus did not have an accurate sense of what the communities really wanted or needed in order to be able to design a plan that had meaning and importance to the communities. This lack of ownership (and understanding of the plan contents) combined with a lack of initiative on the part of local governments caused problems throughout the process.

2.12 Under both loans, the subprojects selected during the medium-term planning process were often observed by the audit mission to be somewhat ad hoc.²⁵ Project provisions required

23. The GOI notes that, when properly managed, central government consultants working with local governments should be sensitive enough to take local opinions sufficiently into account to create strong ownership.

24. The GOI correctly points out that had local government wished to be more actively involved, this would have been permitted.

25. This finding concurs with the EJB ICR (p v, *para* xiv), which points out that “A further drawback [of integrated planning] was the inadequate attention to preparing sectoral master plans as the basis for investment programs, and a

investments over a certain size to receive careful technical review. Although the intention was quite the opposite, this stipulation actually created an incentive for cities to build small and poorly planned works. The SARs specify that roads are to be built in urban areas, but the audit mission noted roads built in rural areas to “spur residential development.” Even eight years after their construction, little residential development could be noted (Bangli, Bali—EJB; Bitung, Sulawesi—SIJ).

2.13 The audit also noted negative environmental impacts of some subprojects visited. In one case, in Bitung, Sulawesi loan proceeds helped to finance the construction of an industrial park on top of a four-meter-deep marshland on the water’s edge. While the Bank only financed an access road, the park would not have been built without its commitment to the road. This ecologically important zone had been protected by mangroves, which were also destroyed in the process.²⁶

2.14 The IUIDP approach limits the planning focus to seven or so sub-sectors, including solid waste, sanitation, water supply, urban transport and traffic management, roads, drainage, and *kampung* and market improvement programs, depending on the project. Even though the projects were already exceedingly large and complex, the fact that they did not cover all sectors made planning a municipal budget difficult. This not only made it difficult to plan a city strategy, but many officials complained that it also led to a neglect of those projects not covered under the loan but still needing attention (including infrastructure works not included in the city’s medium-term plan). In addition, the neglect of other areas often caused problems with the infrastructure built with project funds. Mining, unregulated and intensive construction of housing on hillsides, and the lack of an adequate waste disposal system ended up clogging drains and endangering the water supply systems of several cities.

Organizational Integration Difficulties

2.15 The attainment of broad, integrated goals was compromised by complex implementation arrangements and lack of communication.²⁷ For example, project coordination activities in the SIJ UDP involved 9 local governments, 12 water enterprises, 5 provinces, more than 10 central government agencies, and several consultant teams. The central inter-ministerial Coordination Team for Urban Development (TKPP), supported by a large secretariat, provided coordination in Jakarta for the entire GOI urban program, while parallel inter-agency provincial and local teams were formed to coordinate the programs in each jurisdiction. These were supported in EJB with provincial management and technical units, and in SIJ with the overall Project Management Unit with appropriate local teams in all cases. Even though communication lines had been established by design, timely and effective communication was rare.²⁸ The Borrower ICR for Bali

tendency to focus instead on short term needs on an ad hoc basis.” The ICR also points out that “The majority of the investments (over 70 percent) in urban roads and drainage were small...” attachment to Table 9, EJB ICR, p 29.

26. EASUR comments: “In our view the environmental issues noted in the draft PAR are evidence primarily of the incomplete legal, regulatory and institutional frameworks in Indonesia during the implementation of these projects....[In] both projects...we helped these provinces and local governments get started, but GOI was still trying to get new legislation, regulations and the BAPPEDAL institutions in place while these projects were being implemented, so some incomplete addressing of these issues are to be expected at the time.”

27. EASUR ascribes delays in getting the new arrangements and capacities in place to “teething problems in the adjustment of roles and responsibilities, which normally could be expected.”

28. EASUR objects to the PAR’s not specifying that “one of the most important strategic differences between the two projects [was] in terms of supervision/oversight.” Field visits could detect little difference in the functioning of the two systems, at the Region’s request the following text is included here: “From the outset of preparation the Bank and central GOI understood clearly that having a close, working relationship with all 45 units of local government (excluding Surabaya covered in a separate project) in East Java and Bali provinces would be practically impossible. It was thus essential to the success of the EJB project that provincial intermediation capacities be developed, and the

complained of difficulties due to lack of communication and coordination between IUIDP organizations at different levels of government.²⁹

2.16 Local-level project participants in both UDPs observed that sector providers championed their own projects and did not concern themselves with what was happening in other sectors, leading to uncoordinated and therefore wasteful investments. Municipal staff that met with the audit mission complained that each sector had different timing, schedules, project managers, and funding schedules, and that this made it difficult to coordinate efforts.³⁰ On more than one occasion officials involved in coordinating efforts remarked that it was common to see a water distribution system built and only much later would the required pump be installed. Another more egregious example mentioned by local officials was that of the septage treatment plant that was built without the water connection necessary to make the plant function. As of the audit mission three years after construction was completed, the water connection had not been made, the septage treatment plant lay unused, and staff were still uncertain about when water would actually be made available. Similarly, new roads were built even though it was known that water pipes would need to be laid shortly thereafter. Components were sometimes fully implemented before staff were given the training they were supposed to receive beforehand. The lack of coordination among agencies also created confusion regarding hierarchies and responsibilities, which resulted in the duplication of effort and the neglect of maintenance.

Operations and Maintenance

2.17 The audit mission visited several infrastructure components where the facilities built with loan proceeds now stand in disuse. Although EJB was the first Bank attempt to deal with O&M with a loan covenant requiring local governments to budget agreed minimum O&M funds each year, facilities abandoned due to a lack of attention to (and budget for) maintenance and management were nevertheless found. Most project drains inspected were clogged with garbage and silt or, much worse, so totally buried/filled in that an observer could be persuaded that they were nonexistent—this only three years after project completion.³¹ In Kintamani, Bali, half of the installed water distribution infrastructure has fallen into disuse due to lack of operating funds. Residents are no longer receiving water, the pumps only run four to six hours per day at just over half the efficiency they did directly following the project, and the water company has turned off

provincial government lead the project preparation and implementation while serving as the focal point of Bank and GOI supervision and reporting. Again, this was a first for this project in Indonesia, and it worked relatively well. While in the SullrJa project the provincial governments were not seen as capable of fulfilling this role and the numbers of local governments were small enough that a more typical, free-standing Project Management Unit was created for this project.”

29. “Both provincial and local governments stated that they have not achieved satisfactory achievements in sector coordination and integration among the IUIDP supporting organizations, the [provincial and local project planning, finance, and management offices]. There is also no proper communication between [the Urban Development Coordination Team/IUIDP Implementation Management Group, BAPPENAS] and provincial and local governments” (Borrower ICR, Bali, p 86).

30. The GOI notes that an effort was made to integrate funding for the various sectors.

31. Part of this might be explained by the effects of the financial crisis, but Bank staff familiar with Indonesia remarked that “All the trends of low cost-recovery, poor design/construction, non-existent O&M and corruption in implementation were well established before [the crisis].” EASUR believes that project efforts to plan for O&M “made major strides in clarifying for local decision-makers both the needs and effectiveness of their O&M funding.... We believe this aspect of the EJB project is not correctly portrayed in the draft PAR which seems to focus on the ‘snapshot’ of O&M problems observed during July 2000 field visits, when conditions were severely impacted by the crisis... while ignoring the relatively huge impact of the project in changing local understanding, budgeting and O&M performance in at least ‘first batch’ localities from 1992-97 (until the onset of the crisis).”

the electricity in four of the five purification levels. The poor performance is due to three factors: a lack of adequate management, poor maintenance, and budgetary shortfalls.³²

2.18 These discoveries are surprising given the emphasis placed on O&M in these projects. In the EJB UDP, O&M expenditures amounted to \$106.1 million, or 26.5 percent of the total project cost (ten times the proportion of funds spent in SIJ, which amounted to 2.6 percent of total project cost).³³ The funds were meant to (a) improve O&M of existing facilities or services, and (b) initiate necessary O&M for new and rehabilitated infrastructure and services developed during the implementation period of the project.³⁴ According to the EJB appraisal document, “These additional O&M expenditures, with the associated local capacities to execute improved O&M, represent *one of the most important program implementation targets* (emphasis added).”³⁵ One of the reasons for this high expenditure included expensive and advanced technical assistance that overshot the institutional capacity of local governments according to one Bank staff member. This technical assistance included the installation of and training for a computerized maintenance management system, which, as discussed in the next section, was not implemented in many cases, or it was set up but then abandoned at project close.

2.19 Both projects substantially achieved their physical objectives, but if the institutional capacity to carry out O&M programs is not also built, the infrastructure constructed will speedily deteriorate. The EJB ICR mentions that the septage treatment plant (IPLT) in Denpasar was “well laid out, satisfactorily constructed, and is one of the few working septage plants in Indonesia.” The audit found that this plant can no longer be used. The audit mission in July of 2000 found the contents in the system dried out and solid, and untreated effluent being dumped directly onto agricultural lands.³⁶ Not only has this subproject created a negative environmental impact, but the physical investment is now at risk. The impacted contents make it extremely unlikely that operation can be restored. The SIJ ICR correctly observed that, the achievement of physical objectives, while important, cannot be sustained unless these are supported by corresponding progress in institutional capacity and changed attitudes that are oriented toward service delivery. A lack of institutional capacity and training about procedures and treatment (noted by Bank staff and several government officials) compromised the attainment of project objectives.³⁷

32. The water enterprise responsible for this complex has not received funding from the follow-on Bali Urban Infrastructure Project *inter alia* because of the failure to raise tariffs to levels high enough to cover electricity and other operating costs.

33. This striking difference can be partially explained by the fact that project designers believed that EJB possessed the institutional capacity necessary for O&M and that the region has more (and older) infrastructure to maintain than SIJ. (\$19.46 million was the original cost estimate for O&M in SIJ.)

34. The latter included the installation of the Performance-Oriented Maintenance Management Systems, the provision of training and advisory support to local and provincial staff in the programming, budgeting and management of O&M activities.

35. EJB SAR, p 33-4.

36. According to local officials, the pump kept breaking and parts were excessively difficult to procure. The system was abandoned and a gravity-fed system is being installed. The June/July 1995 Supervision Mission Aide-Memoire states “The plant became inoperable after about six months due to breakdown of the two pumps. Disposal of the sludge has since been by direct dumping to effluent ponds in a very environmentally unfriendly fashion....It was also disappointing to note that the system has not been cleaned out since the pumps became inoperative. As the contents dry out and become solid, it will be extremely difficult to clean-out and restore operation” (Annex 1, Water Supply and Sanitation Issues, p 2).

37. EASUR comments: “We find the discussion of O&M issues in the PAR to be unfair and lacking perspective on the actual conditions in Indonesia over the time period of the project and since. The budget structure and incentives for local governments (still until today) have been to minimize ‘routine’ expenditures from which most O&M costs are financed, and to maximize ‘development’ expenditures (projects, etc.); e.g., it was (is) common for local governments to ignore drainage maintenance for a couple of years until silt and debris clogged drains sufficiently to justify seeking

Institutional Development Impact

2.20 To increase institutional capacity for service delivery, the IUIDPs included the preparation of several institution-building elements in their plan, such as medium-term plans,³⁸ Performance-Oriented Maintenance Management Systems,³⁹ Revenue Improvement Action Plans,⁴⁰ and management support for water enterprises. These components had varying degrees of success.

2.21 *Medium-Term Plans.* The medium-term municipal expenditure plans required by the audited IUIDPs are an example of a critical failure to augment local government capacity. In many instances these 5-year plans were prepared by consultants who, not familiar with the local situation, often designed inappropriate plans. For instance, in EJB, the consultant in charge of Program Preparation and related Start-up Support (Batch II/III) and the preparation of Medium-Term Plans (Batch III) for Local Governments was assessed as *unsatisfactory* during the GOI's self-evaluation process because: "The respective local governments were not involved during [Medium-Term Plan] preparation which caused mistargeted programs."⁴¹ The 17 local governments of "Batch III" in East Java were not prepared in time for any significant investment to occur during EJB, and consequently they were mainly prepared for EJ2.

2.22 These plans were meant to be dynamic documents to facilitate vision, but there were no incentives to revisit the documents and adapt them to changing situations and needs. In fact, the lengthy paperwork process to change the plans was regarded by many consulted as a deterrent. If plans were not modified in the face of changing circumstances, municipal decision-making then ran the risk of relying on an irrelevant plan. Officials in EJB reported that some changes (updates) were made by municipalities in East Java, but much of the time municipalities limited themselves to simply doing what was already in the plan. In SIJ, plans, once submitted were rarely changed, even when obviously needed. The fact that these plans were not easily changeable led to a certain lack of dynamism and adaptability of the projects. IUIDP contributions to improved urban planning will not have the desired impact until participating cities engage in goal setting and prioritization.

2.23 *Performance Oriented Maintenance Management System.* All participants consulted commented that the computer program developed under the project to monitor O&M was either never adopted by participating cities, or it was adopted and then dropped once the project was over.⁴² An IUIDP expert commented that the system could not have been readily implemented—it identified problems, but there was no institutional capacity to deal with the problems. O&M is a difficult subject everywhere, but as one Bank staff member pointed out, "You can't fix it with a fancy accounting system (yet the system had to be fancy to deal with the situation)."

provincial or central assistance for a major 'drainage rehabilitation' project bringing outside funds, rather than spending their own routine funds for drainage O&M."

38. PJMs

39. POMMS

40. RIAPs

41. Borrower ICR, Bali. Table: "Studies Included in Project."

42. Reasons given for this included the obsolescence of computer equipment and lack of money to update systems, and the fact that the government already had its own system in place—and several officials expressed their intention to return to their own system. EASUR does not agree, however, noting, "A simplified, manual version of the POMMS was developed and piloted with some of the smaller local governments to overcome the complexity issue with the original system; thus, portraying POMMS as 'expensive and advanced TA that overshoot the institutional capacities of LGs' [local governments] is both incorrect and unfair."

2.24 *Revenue Improvement Action Plans.* The Revenue Improvement Action Plans had some success in the EJB project and the ICR reports that “the local revenue generation target was substantially achieved,”⁴³ (although the SIJ ICR hints that other factors than project actions were responsible for improved revenue flows in Sulawesi).⁴⁴ Unfortunately, according to the borrower, “the sustainability of RIAP heavily depends on the supervision and assistance of the consultant, especially in preparing the revision and adjustment of annual RIAP targets.”⁴⁵

2.25 The EJB UDP, according to the ICR, “contributed to strengthening local government institutions in various aspects of IUIDP, primarily through learning on the job, with support from various consultants.”⁴⁶ Frank discussions at the various sites visited revealed that, most of the time, consultants ended up doing all of the work. The Bali Borrower ICR states, “Dependency of all levels of governments on consultants is still high almost in all areas of urban development and management.”⁴⁷ Local and provincial governments in Bali reported that there was a “low degree of sustainability of [the] system (POMMS, RIAP, PFAMS) without continuity of consultant’s involvement.”⁴⁸ They commented that they do not have ample opportunity to learn and apply those consultant-installed systems.⁴⁹

2.26 The SIJ ICR pointed out that institutional capacity is not only a function of staff skills and training, but rather a function of the environment in which they work (e.g., incentive structures) and the result of effective linkages between various government agencies, government levels, and the community. Unfortunately, these were fragile. The overall attempt at capacity building in the two projects was a bit thin on the ground and even with the support of Bank staff, institutional development efforts did not have the hoped-for effect.

Supervision

2.27 The newness and scale of the IUIDP endeavor created high supervision demands. In EJB, Bank supervision of physical works was undertaken “on a sample basis,” “given the geographic spread and the number of sectors involved.”⁵⁰ It is questionable whether the supervision budget was adequate to the scale of the task as several problems relating to a lack of supervision arose in both projects.

2.28 A provincial-level planning official pointed out that the poor quality of supervision was a major hindrance to the EJB UDP. In the Klungkung water sub-project (EJB), the contractor deviated from location specifications, building the system along a river because it was easier and quicker to do so. After the infrastructure was washed away—because the river regularly floods—it had to be completely rebuilt elsewhere. This lack of supervision in the EJB UDP led to the total

43. ICR figures show only the growth rate from 1995/6 to 1996/7.

44. “where local revenue rose significantly, it is not conclusive that the Revenue Improvement Action Plan contributed to the change.” SIJ ICR, p iii, para vii.

45. Borrower ICR, Bali, Ministry of Public Works Directorate General of Human Settlements, Bali. Final Report September 1997: p. 81.

46. EJB ICR, p 5, para 25.

47. Borrower ICR, Bali, p. 83.

48. Borrower ICR, Bali, from Table 2.10.1 “Perception of Local and Provincial Government Regarding the Quality of Projects Completed and Effectiveness of TA” p 74.

49. Borrower ICR, Bali, p 83.

50. EJB ICR, p 9, para 42.

loss of a \$2 million investment, and the need for another \$2 million to rebuild.⁵¹ Another example reported to the audit mission was an instance where, due to poor supervision, PVC (polyvinyl chloride) pipes were used in a transmission main along a main road to save money (although galvanized had been called for). Poor installation and pressure from vehicular traffic led to breaks and separations. These problems might have been avoided with proper borrower supervision.⁵²

Water Enterprises

2.29 Water supply was allocated the largest portion of infrastructure investment in both loans.⁵³ Technical assistance was provided to improve the viability of the existing water enterprises and several of their activities were supported in order to make them more entrepreneurial. Although many water enterprises increased the production of water and connected more families to the water network, locally collected revenues still only cover a small percentage of the companies' expenditures.

2.30 Many SAR targets were not met though the EJB ICR in particular argues the outcome was successful, stating: "in general, all participating [water enterprises] exceeded SAR targets for water production and number of connections."⁵⁴ (However, EJB ICR Table 6 shows that 32 percent of the water enterprises did not meet water production targets,⁵⁵ and Table 5 shows that targets for house connections were not met in either East Java or Bali⁵⁶).⁵⁷

2.31 Inconsistencies aside, physical targets (e.g., number of connections made) often are not the central issue. Even if all of the physical targets had been met, cost recovery, financial data, institutional capacity, and the bottom line can be crucial to the utility of an investment. For example, customers can be connected, but that does not mean that services are necessarily being delivered. Kintamani, Bali is one example of a large investment in physical infrastructure that was successfully built, but that is now lying in disuse due to the enterprise's lack of institutional capacity (described above). Even if we accept the ICR statement that "The project generally

51. EASUR believes that the emphasis of this PAR, "...should be on the importance of establishing the decentralized capacities, rather than on the (relatively) small failures which occurred while this was being achieved."

52. EASUR explains this by noting, "the central GOI sector unit for water supply developed the Klungkung system before the supervision consultants for the PPMU (technical quality control unit) were mobilized."

53. \$42.8 million allocated for water supply infrastructure in EJB (Table 1: "Project Cost Summary, Staff Appraisal Report, EJB UDP," p 21), and \$46.3 million allocated for water supply infrastructure in SIJ (Table 2: "Project Cost Summary, Staff Appraisal Report," SIJ UDP, p 19).

54. EJB ICR, p 20. See also EJB ICR, p 2, para 10.

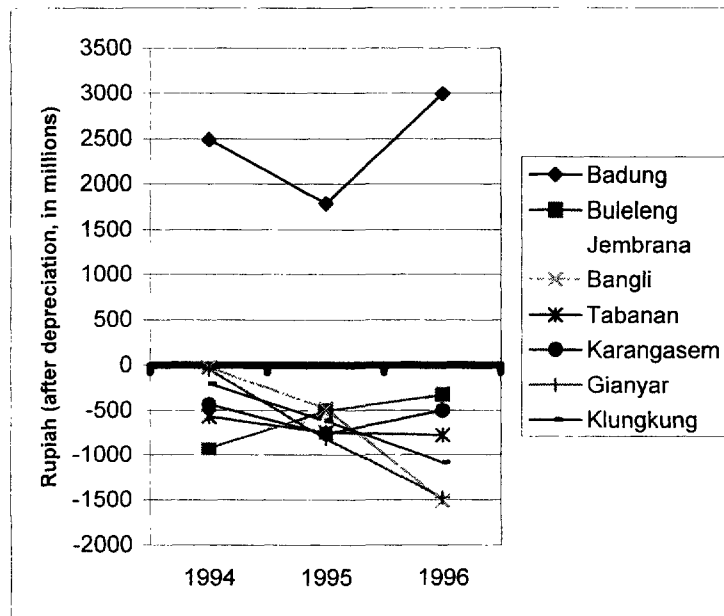
55. ICR Table 6: "Key Performance Indicators for Project Operation, Main Achievements of Participating PDAMs."

56. East Java—Targeted: 11,237, Actual: 8,580 Bali—Targeted: 21,575 Actual: 12,900. Table 5: "Key Indicators for Project Implementation," EJB ICR, p 16. The EJB ICR also notes: "The significant variations are due to the programmatic nature of the project; at appraisal, investment volumes were estimated, based on assessments of the investments in the first batch of local governments. Actual investments reflect the changed conditions and the priorities at the time of finalizing annual development programs." If one looks at SAR estimates versus the actual outcome, 68 percent did not meet the target for staffing ratios (15 out of 22).

57. EASUR comment: "The continued focus of the PAR draft on the ICR summary tables of achievement versus targets seems to miss the major point of this programmatic operation. The intent of establishing the 'targets' for the program at appraisal based on the first batch preparation only was to have an estimation of the overall scope of the full program needed in the two provinces and enable measurement of progress toward meeting these needs, but with no expectation that the initial project would fully complete this program. Indeed, one of the purposes for including these summaries in the ICR was to demonstrate that the 2nd East Java (EJ2) and BUIP projects were needed even in light of progress achieved during the initial EJBUDP."

achieved its targets of water production and service connections,⁵⁸ all PDAMs in Bali, except Badung, suffered losses for the years 1994, 1995, and 1996 (see Figure 1). Furthermore, in all but one of those, losses increased over time.

Figure 1: Bali PDAM Profits and Losses (EJB)



Data Source: Borrower ICR, Bali.

2.32 The Bali Borrower ICR also reports that, except Badung, the project economic internal rates of return (EIRRs) and net present value (NPV) of the other water enterprises in Bali were negative and the number of customers did not meet the SAR targets. This data is apparently not taken into account by the EJB ICR assertion that, "Although no economic analysis was carried out for Bali water supply investments at project completion, they should be considered *economically viable* as physical targets set at appraisal, e.g., number of connections, volume of water sold, unit operating costs (upon which the appraisal economic analysis was based) were largely met"⁵⁹ (emphasis added). Out of the data available for eight service-related indicators,⁶⁰ only 45 percent of the SAR targets were met in the 14 PDAMs in East Java (although 74 percent of the targets were met by the 8 PDAMs in Bali).

2.33 In general, there were inefficiencies built into the water enterprises. There were persistently high rates of unaccounted-for water (rates reached as high as 66 percent), and poor collection of water bills. Fees were charged according to usage as long as the meters were operational. Owners of broken meters were only charged for average consumption. This created an incentive for consumers to break their meters to lower their bill. Adding to inefficiencies, many unconnected customers were waiting for service but not receiving it even though the water enterprises were not operating at full capacity. According to EJB project files, in one area only 55

58. EJB ICR, p 2.

59. EJB ICR, p 30, para 8.

60. The eight categories include: volume produced, volume sold, percent unaccounted for water, services ratio, number of connections, staff per 1000 connections, days accountable receivable, and average tariff.

percent of the available water was being used, while 400 customers waited to be connected. The availability of central government grants created a perverse incentive (when local governments cared little for providing good service) since, as losses increased, municipalities could actually receive more grants. Full cost recovery goals proved way too optimistic. This is recognized by the EJB ICR, which noted that, “incentives to ensure compliance of individual [water enterprises] to loan covenants were not built in.”⁶¹

2.34 Single-sector investments should receive more consideration for the less developed areas of the country. The Irian Jaya portion of the SIJ UDP, which involved only the water sector, performed well—especially given that financial and institutional capacity in Irian Jaya are low and unmet demand for water service was greater than it was in the other project areas. This water system rehabilitation and development investment sub-project increased system production capacity and sales, improved service reliability and water quality, and increased service coverage. Total served population exceeded its target by 17 percent over the SAR 1996 estimate of 295,010 people.

Poverty Impacts of the *Kampung* Improvement Components

2.35 *Kampungs* are an integral part of the Indonesian urban scene. They are densely populated and primarily low-income neighborhoods. They are located in strategic parts of many cities that provide good access to employment for their residents. *Kampungs* are often found in the midst of more affluent and expensive neighborhoods, bordering larger government facilities, near shopping areas, and in areas that often flood. In many cases, they are pockets of poverty within a larger and better-off neighborhood that provides services to the *kampung* residents. Unless there has been a neighborhood upgrading project recently, *kampungs* often lack elements of basic infrastructure such as walkways, storm drains, and sewerage.

2.36 The EJB SAR states that the first element of the Bank strategy is to “improve service levels in a regionally balanced fashion and *particularly for the poor*”⁶² (emphasis added). To attain poverty relief goals, IUIDPs prescribed a KIP component.⁶³ The fact that KIP was a part of IUIDP, yet not necessarily appropriate for all cities, led to untargeted investment. The audit mission observed that in both EJB and SIJ (and this could probably be said for many IUIDPs in Indonesia), most *Kampung* Improvement Program (KIP) developments took place in what is now low-density middle- to upper-class neighborhoods. Some KIP sites were in areas where half of the land was vacant (and being held, unused, for speculation). In such areas, the new amenities probably guarantee that low-income families will never be able to afford to live there. Municipalities (perhaps) felt the need to implement the KIP components, but were hard pressed to find an “un-kipped” low-income neighborhood that was sufficiently organized and otherwise ready to improve (although some cities forwent the KIP component altogether). Municipalities in Bali that did not want to miss out on the investment opportunity provided by the loan had a hard time finding low-income neighborhoods with sufficient population densities (to meet GOI KIP density norms).

2.37 Many of the difficulties described in this audit are common to almost all urban projects in Indonesia, such as limited knowledge transfer when using consultants to “increase local capacity,” a lack of follow-through for operations and maintenance, the problem of “transfer upon

61. EJB ICR, p 9, para 41.

62. EJB SAR, p 14.

63. KIP improvements received more funding than solid waste management, sanitation/sewerage, or market infrastructure improvement.

training” where those who receive training are transferred up the hierarchy and out of the office that was meant to benefit from the acquired knowledge, and difficulties maintaining adequate borrower supervision of project works. Many other difficulties, however, are unique to IUIDPs. Such problems mentioned include: a perverse incentive for cities to plan several small and somewhat ad hoc projects; lack of local ownership of medium-term plans; varying institutional capacity from city to city, but a need to include all cities regardless of readiness; failure of plans to be dynamic documents and to change as needs change; and a forcing of KIP planning onto areas that did not technically qualify for KIP-type improvements (not dense enough, or income levels not low enough).

3. Assessment of Performance

3.1 IUIDP was the joint operational approach agreed upon by GOI and the Bank to address the highest priority urban development objectives for the country. The IUIDP projects were highly relevant to Bank and borrower priorities. They were consistent with the CAS, the Statement of Policies for Urban Management (1987) and applicable national five-year plan. Because of its multi-sectoral, decentralized planning approach, IUIDP was a major departure from earlier sectoral approaches, and the two projects did contribute to a paradigm shift—from central to local responsibility—for urban infrastructure. Planning and building the infrastructure did create support for decentralization, and begin a more holistic way of looking at infrastructure development and city planning.

3.2 While enthusiasm for an integrated approach to development is high within the local governments visited, and most of the physical infrastructure for the two projects was successfully built, the projects suffered several shortcomings. Attention to operations and maintenance was lacking. The influence of the financial crisis needs to be placed in the context of the \$96.2 million budget for O&M in EJB, especially considering the relatively low cost of simple, yet system-saving measures, such as clearing drains. The effort expended (by the two evaluated projects) to provide increased household access to safe water was complicated by perverse incentives and inadequate attention to water system management. Even the modest improvements achieved are diluted because of poor targeting—in the sense that areas where drainage was built apparently did not receive full sanitation coverage: in many places it could be observed that uncollected waste plugged the new systems. Factors that affected the projects’ sustainability are sub-optimal institutional progress, and the low resiliency of project benefit flows to the risks posed by the economic downturn and inadequate maintenance.

3.3 Institutional development objectives were also met but partially. Improving urban infrastructure expenditure programming, financial planning, and information management in the local government units proved to be another problem area. Local governments tended to see the longer-term planning exercises more as a hoop to jump through than as a tool they intended to use. Clearly, local governments’ capacity to prepare and execute annual O&M programs increased little. Even where water enterprise revenue generation improved, financial management remained weak as revenues remained below water system expenditures. Nevertheless, both projects assisted decentralization efforts nationwide, and, as will be discussed further below, follow-on projects have been modified in a manner that indicates important lessons from the early IUIDP projects have been learned. Each project is rated separately below.

East Java/Bali

3.4 The audit rates project outcome as moderately satisfactory, sustainability as unlikely, and institutional development impact as modest. This differs from the ICR, which rated overall outcome of the project as satisfactory and sustainability uncertain. Although the project achieved some of its objectives, and relevance was high, there were several significant shortcomings.⁶⁴ Two regions with much of the nation's wealth and talent, East Java and Bali have a high potential for successful project implementation. Nonetheless, the audit found several disturbing trends, including costly errors due to a lack of supervision, and infrastructure lying in disuse or, worse, built twice. Large investments in O&M were lost due to an overestimation of local capacity to handle complicated procedures. The lack of institutional capacity-building is both a problem in and of itself, and a contributor to poor sustainability, as is local hesitancy to undertake timely maintenance. Continued inadequate attention to system maintenance indicates the situation will likely continue to deteriorate, hence the sustainability rating of unlikely.⁶⁵

Borrower Performance

3.5 Difficulties early in the project are understandable considering this was a pilot project (although the project was not of the scale normally associated with a pilot endeavor, it was the first of nine IUIDPs)—the borrower's performance was satisfactory.

Bank Performance

3.6 The Bank's performance was satisfactory. Significant levels of support were provided to in-country staff attempting to confront a broad range of the country's most intractable urban problems all at once. More should have been done earlier to tackle the O&M deficiencies, and the ICR could have been more frank and lesson-focused.

Sulawesi/Irian Jaya

3.7 The audit rates project outcome as moderately satisfactory, sustainability as unlikely, and institutional development impact as modest. Relative to the ICR ratings, these ratings are unchanged. (The ICR overall outcome rating of marginally satisfactory is essentially equivalent to moderately satisfactory.) Although the project achieved most of its physical objectives efficiently, and relevance was high, there were significant shortcomings—infrastructure had seriously deteriorated, maintenance was not being performed, and institutional weaknesses persist.

Borrower Performance

3.8 Borrower performance was satisfactory. GOI staff did not fully respond to the challenges posed by the institutional weaknesses of cities in this project. On the other hand, progress at the local level was remarkable. Developing an understanding of a new project concept, IUIDP, and putting it into practice was particularly demanding for municipal staff in this region. However,

64. The Region objects to this downgrade on the grounds that project shortcomings were not significant.

65. It was impossible not to change this rating. The OED rating system has been modified since the ICR was reviewed. "Uncertain" is no longer used, and options are limited to highly likely, likely, unlikely, highly unlikely and not evaluable. The project performance described in this report supports the rating assigned (unlikely) far more than it does a rating of likely.

the starting line was further back for SIJ than for most IUIDPs, meaning that even though progress was substantial, the end result was still lacking.

Bank Performance

3.9 The audit rates Bank performance as satisfactory, upgrading the ICR rating of marginally satisfactory. Bank preparation assistance was extensive. The Bank's urban strategy provided a framework for identifying the project, and staff responded sensitively to GOI priorities. The ICR was particularly analytic and forward-looking.

4. Conclusions and Lessons

4.1 Expectations that municipal practices would change rapidly were unrealistic. *De jure* decentralization takes place rapidly, *de facto* changes in practice need to be seen as a long-term goal that involves not only the building of physical infrastructure, but also the building of institutional and social capacity to support those physical investments. City infrastructure and investment planning is not yet where project designers hoped, but external events are highlighting the importance of the integrated planning concepts nevertheless.

4.2 In many cases local governments did not originally have the capacity, willingness, and/or incentives to accept the responsibilities given them under decentralization and the IUIDP projects that supported it. That is changing slowly, however. Economic crises have at least one positive impact: they provide enormous incentives for better financial management, and penalize the tendency to (expensively) focus on short-term needs on an ad hoc basis.

4.3 Despite both being early IUIDPs and having faced many difficulties in common, the two projects were quite dissimilar. They took place in radically different contexts, had subtly distinct structures, and made dissimilar advances in the decentralization agenda. Important commonalities also exist. IUIDP was a good learning experience for medium-sized cities. Despite significant early resistance, local officials are now all for the idea of holistic planning, although some still see IUIDP more as a source of additional money than as the bearer of tools they want to use.

4.4 Among the less positive aspects of IUIDP was the proscription of generic standards drawn from estimates for medium-size cities, that wound up creating problems for smaller and larger cities all over Indonesia. Within the project files, staff memos suggested that IUIDP be reserved for an approach that can be used to help cities to prioritize planning, broaden monitoring, and improve investment decisions, but that it be dropped as an approach to implementation. Such a sweeping recommendation is beyond the scope of this evaluation. It is true that IUIDP was not particularly well-adapted for smaller cities and towns, and not enough allowance was made for the influence of local conditions on implementation. Designing integrated plans is a good idea, that is, putting together an overarching plan that takes into account everything that IUIDPs take into account. Clearly, smaller projects that can then be implemented independently but simultaneously would be more manageable. More also needs to be done to create the right incentives for local governments.

4.5 Despite implementation difficulties, the audit did observe a certain amount of institutional learning and borrower enthusiasm for the IUIDP concept. These two projects must be seen as the first in a series of attempts to improve municipal service delivery—to quote a project participant: “Decentralization is a long-term institution-building effort. There are no shortcuts to decentralization and integrated planning.”

Lessons

4.6 *Identify the minimum necessary conditions for success.* Early Bank urban projects were overly comprehensive: they tried to do too much and involved too many agencies. Inter-agency coordination was usually problematic, and sequencing of activities across sectors sometimes led to crippling delays. OED evaluations of that time often stressed over-complexity as the reason more was not achieved. As a result of the difficulties, urban projects became increasingly focused, and more recent evaluations suggest that eventually they became too much so.

4.7 In the case of the storm drainage component, minimum necessary conditions include parallel garbage collection and drainage efforts. As happened in many communities, uncollected garbage blocks storm drainage. In some cities, more was needed: regulating soil erosion from hillside construction would have been helpful. In others, mining wastes were a problem that should have been taken into account to prevent the irreparable loss of storm drainage. Better sequencing could have helped overcome this problem—for example, waiting to construct storm drains until adequate refuse collection happens routinely. Conversely, designing systems that cannot be blocked by refuse, and that trap it in easy to service locations, is another solution. A recent OED evaluation in several Brazilian cities⁶⁶ discusses the use of refuse traps, concluding that for most communities, the basic package needs to include and sequence four activities (water, sewerage, storm drainage, and garbage collection) or long-term sustainability is put unnecessarily at risk and potential health benefits diluted.

4.8 *A rolling planning process requires incentives for updates.* The medium-term municipal plans required by IUIDPs were intended to be living documents in the sense that cities were expected to revisit them periodically, adapting them to changing situations and needs. It will be recalled that in SIJ plans were rarely changed, even when obviously needed. This may be a case where more care needs to be taken to ensure that ownership exists or incentives for the first few exercises need to be built in. Until goal-setting becomes part of the planning process, the cities will be engaged more in *programming* than in *planning*.

4.9 *Pressure to move fast, provide broad coverage, and cover a large geographic area were counterproductive.* When project leaders were pushed to plan IUIDPs throughout Indonesia, areas not ready to be involved were included anyway. Wanting IUIDP to be a national program may be commendable, but testing the concept with one pilot project might have been more prudent (whereas rolling out so many untested projects at once was not).⁶⁷

4.10 *Uninterrupted attention to the environment is required in large projects with multiple components lest damaging activities escape the requisite scrutiny.* The projects included mechanisms for identifying environmental problems and sometimes they worked quite well. Unfortunately, problem identification worked better than enforcement and remediating actions. In some cases reports were prepared, but they sat on desks and occasioned no response. The audit notes the building of roads in fragile coastal zones, the filling of important wetlands and the dumping of untreated septage. While these are small-scale occurrences relative to the size and

66. Performance Audit Report for the Water Project for Municipalities and Low-Income Areas (Loan 2983-BR).

67. EJB was deemed a “pilot project” in the ICR, but no mention of “pilot” could be found in the SAR. EASUR notes, “We feel that limiting the number of SullrJa local governments participating, and starting EJB with only 13 local governments in the “first batch” (9 in East Java and 4 in Bali), represents an appropriate “piloting” response by the Bank to GOI efforts to make the IUIDP approach national policy as quickly as possible. We feel that the projects represent a prudent and responsible approach to assisting GOI to explore implementation modalities for their new policy framework...”

number of works undertaken under the loan, the fact that just a few visits uncovered this problem suggests that they may not be isolated occurrences.

Lesson-Learning Reflected in the Follow-on Projects

4.11 To a significant degree lessons learned in the audited projects are being taken into account in the follow-on projects. In the case of the EJB UDP, two follow-on projects are currently being implemented—the Second East Java Urban Development Project EJ UDP II (Loan 4017-IND) and the Bali Urban Infrastructure Program (Loan 4155-IND). The follow-on to SIJ is the Second Sulawesi Urban Development Project (Loan 4105-IND). It covers the 9 original towns, plus 32 additional towns in all four Sulawesi provinces. *Inter alia* it emphasizes decentralization, greater integration of environmental considerations in urban development management, and the strengthening of local government institutions, and community participation in urban investment programs.

4.12 The three follow-on projects have made fundamental changes. They are more environmentally sensitive: the Quality Assurance Group rated the Bali project one of the two best projects evaluated in 1997 for quality at entry and it was rated environmental best practice. The BUIP environmental management and monitoring plan is included in the Bank's environmental best practice database.

4.13 The follow-on projects are also more rigorous and realistic about cost recovery: In the current East Java project, 65 local government requests for funding have been refused due to proposed projects' noncompliance with the relevant provisions of the loan agreements. The follow-ons have smaller geographic scope (except Sulawesi II); all address environmental issues more effectively, especially BUIP. The medium-term plans are now a more flexible program and budget document, and they incorporate an annual review mechanism. Local participation is also much more active and integrated. In some areas project staff now hold monthly forums with the community, which should lead to greater local ownership.

Annex A. Basic Data Sheet

INDONESIA EAST JAVA/BALI URBAN DEVELOPMENT PROJECT (LOAN 3304-IND)

Key Project Data (amounts in US\$ million)

	Appraisal estimate	Actual or current estimate	Actual as % of Appraisal estimate
Total project costs	360.5	400.4	

Cumulative Estimated and Actual Disbursements

	FY91	FY92	FY93	FY94	FY95	FY96	FY97	FY98
Appraisal estimate	3.5	31.9	71.4	111.7	152.2	180.3	108.3	180.3
Actual	5.5	10.9	41.1	78.3	116.0	148.4	171.2	173.0
Actual as % of estimate	157	34.0	57.6	70.1	76.2	82.3	95.0	96.0
Date of Final Disbursement: February 9, 1998								

Project Dates

	Original	Actual
Identification (IEPS)	01/88	6/20/89
Preparation	01/90	02/21/90
Appraisal	06/90	06/26/90
Negotiations	08/90	02/21/91
Board Presentation	10/90	03/19/91
Signing	06/90	05/03/91
Effectiveness	06/91	06/25/91
Project Completion	08/31/96	05/31/97
Loan Closing	12/31/96	09/30/97

Staff Inputs (staff weeks)

Stage of project cycle	Actual Weeks	Actual US\$'000
Through Appraisal	159.9	397.0
Appraisal-effectiveness	30.2	73.5
Supervision	177.4	473.5
Completion	16.0	44.6
Total/planned/	383.5	98.6

Mission Data

Stage of project cycle	(month/year)	No. of persons	Days in field	Specializations represented ⁶⁸	Performance Rating		Types of problems
					Implementation status	Development objectives	
Identification/Preparation	2/16/88	5		UM, FA, UP, Ec, PS			
Preparation	6/26/88	6		UM, UP, Ec, PS, WSE, MF			
Preparation	12/13/88	5		UM, ME, UP, FA, FA			
Preparation	3/31/89	7		UM, UP, FA(3), ME, ec			
Pre-appraisal	7/24/89	8		UM, Ec(2), UP, FA(2), ME, PS			
Pre-appraisal	11/30/89	7		UM, UP, FA(2), ME, Ec, PS			
Appraisal	4/6/90	11		UM, UP, FA (2), ME, Ec (2), PS, EvS (2), SS			
Pre-appraisal	12/6/90	7		UM, UP, FA (2), PS, DO (2)			
Supervision 1	6/15/91	6		UM, ME, OMS, PS, FA, EvS	2	1	Mobilization of TA (including final TOR) was behind schedule. Continued delay in completing arrangements for lending to local governments and water enterprises by MOF, mainly because documentation and instructions for "SLA" lending were not completed. Overall delays may necessitate rescheduling of Batch I expenditure programs (PJM).
Supervision 2	11/25/91	7	42	UM, ME, PS, FA, EvS,	2	1	Delays overall necessitated re-scheduling for Batch I expenditure programs (PJM) in april 1992.
Supervision 3	8/8/92	7		UM, ME, Ec, EvS, OMS, FA	2	1	Mobilization of program advisors and other TA support seriously delayed and difficulties anticipated in preparing FY93-94 implementation program and completing Batch III preparation; delays for water supply investments for Kab. Badung (Bali), Kab. Sidoarjo and Gresik (EJ) until financial impact of private sector investment proposals was appraised; same for Surabaya Water Supply. GOI to request extension of 4/1/92 covenant date for water supply tariff status report and adjustment as well as 6/30/92 due date for initial O&M expenditure report.
Supervision 4	11/21/92	5	61	UM, ME, PS, FA	2	1	Same issues as noted in the above mission.
Supervision 5 (Limited)	6/18/93	1	10	FA			Most PDAMs experiencing cost increases and unaccounted for water. Most of the 37 PDAMs in East Java are currently able to cover O&M while most are unable to cover depreciation. Most in Bali cover O&M, but some are not covering depreciation.
Supervision 6	10/30/93	3	23	UM, PS, FMS, FA, EvS, CF	2	1	Continuing uncertainty regarding bulk water source development (I Imhulan

68. E = Environmental Specialist; Ec = Economist; EE = Environmental Engineer; FA = Financial Specialist; IS = Institutional Specialist; ME = Municipal Engineer; O = Operation Officer/Procurement Specialist;

SE = Sanitation Engineer; UP = Urban Planner; WSE = Water Supply Engineer.

Stage of project cycle	(month/year)	No. of persons	Days in field	Specializations represented ^{6b}	Performance Rating		Types of problems
					Implementation status	Development objectives	
				FA, EvS, CE			water source development (Umbulan Springs) for Surabaya Region, including Gresik and Sidoarjo. Issues include: completing the installation of required program accounting
Supervision 7	2/16/94	1	43	UM, IS, FA(2), ME (2), EvS, PS	2	1	
Supervision 8	9/14/94	3	43				
Supervision 9	7/16/95	6	50				
Supervision 10	10/14/95		8				
Supervision 11	5/10/96		29				
Supervision 12	9/24/96		19.5				
Supervision 13	11/1/96						
ICR Mission	7/4/97						

Other Project Data

Borrower/Executing Agency:

FOLLOW-ON OPERATIONS

<i>Operation</i>	<i>Loan no.</i>	<i>Amount (US\$ million)</i>	<i>Board date</i>
Second East Java Urban Development Project	4017	142.7	5/16/96
Bali Urban Infrastructure Project	41550	79.9	May 6, 1997

Basic Data Sheet

INDONESIA SULAWESI/IRIAN JAYA MUNICIPAL/URBAN DEVELOPMENT PROJECT (LOAN 3340-IND)

Key Project Data (amounts in US\$ million)

	Appraisal estimate	Actual or current estimate	Actual as % of Appraisal estimate
Total project costs	188.18		163.95

Cumulative Estimated and Actual Disbursements

	FY92	FY93	FY94	FY95	FY96	FY97	FY98
Appraisal estimate	29.3	46.7	67.9	84.3	96.3	100	100
Actual	4.5	17.63	40.52	63.26	81.50	95.8	95.8
Actual as % of estimate	23.6	37.7	60.0	75.0	84.6	95.8	95.8
Date of Final Disbursement: November 25, 1997							

Project Dates

	Original	Actual
Identification (IEPS)	12/83 – 04/87	12/83
Identification	04/18/88	04/18/88
Preparation	05/88 – 5/89	2/88 – 3/90
Appraisal	6/89	10/90
Negotiations	12/89	4/10-12/91
Board Presentation	3/90	6/6/91
Signing	8/91	8/8/91
Effectiveness	11/91	11/4/91
Mid term Review	6/94	10/94
Project Completion	6/30/96	12/31/96
Loan Closing	12/31/96	6/30/97

Staff Inputs (staff weeks)

Stage of project cycle	Actual Weeks	Actual US\$'000
Through appraisal	98.6	318.6
Appraisal-effectiveness	25.3	60.3
Supervision	147.5	318.1
Completion	9.9	22.8
Total/planned/	281.3	719.8

Mission Data

Stage of project cycle	(month/year)	No. of persons	Days in field	Specializations represented ⁶⁹	Performance Rating		Types of problems
					Implementation status	Development objectives	
Through appraisal	4/87	4		FA, WSE, O, C			
Through appraisal	2/88	6		FA, IS, ME, O, IS, Ec			
Through appraisal	6/88			FA, ME, O, IS, Ec, C			
Through appraisal	3/89			FA, IS, Ec, C			
Through appraisal	7/90			Ec, E, SE, UP, ME			
Through appraisal	11/90			Ec, ME, SE, E, (2), UP			
Appraisal to Board	11/90	6	16				
Full Supervision	11/91	5	8	ME, E, UP, FA, 2 O		1	TA progress slow
Full Supervision	7/92	5	8	ME, E, FA, E, O	2	1	Still slow progress with TA mobilization. TOR under preparation.
Limited Supervision	11/92	4	N/a				
Full Supervision	7/93	2	18	ME, FA	2	1	Watershed management in Irian Jaya working with mixed results; IUIDP component in Sulawesi proceeding more slowly.
Part One: Mid-term Review	06-07/94	6	23	ME, O(2), FA, E, EE	S	S	Part one of the Mid-term Review: Concern over the pace of implementation and quality and sustainability of the physical works; entire project suffers from lack of adequate supervision and monitoring, tariff review of Irian Jay water enterprises need attention; land fill sites location development at city of bitung.
Full	4/95	5	24	E, FA, ME, O			No 590 in file
Limited	7/95	3	6	MRE, FA, O			Civil works deficiencies requiring repair in Irian Jaya; PDAMs problems; training in tariff analysis; ownership of PDAM of Jayapura and increase in tariff.
Supervision							
Limited Supervision	11/95	2	6	FA, O			Need put Wamena system into operation; Irian Jaya PMDU – need for a qualified financial staff.
Full Supervision	5/96	3	10	FA, ME, O	S	S	
Limited Supervision	7/96	1	2	FA			Re-allocation of loan funds for maintenance of drainage sub-projects.
Limited Supervision	7/96	1	0.8	O			Follow up timely completion (December 31, 1996) of Manado PDAM, Baitung, etc. constructions with attention to SLAP arrangements with DP3 of MOF
Limited Supervision	9/96	1	2	WSE	S	NR	Identified watershed issues in the project area
Full/ICR	12/96	5	24	ME, O, FA, E, EE	S	NR	Extensive Review of the status of the project
Limited	4/97	1	1	O			Follow up on the December ICR- Sustainability of project: construction of steel tank works proceeding satisfactorily; but maintenance of new facilities need attention.
Limited/ICR	7/97	3	6	EE, FA, WSE			Sustainability of project

69. E = Environmental Specialist; Ec = Economist; EE = Environmental Engineer; FA = Financial Specialist; IS = Institutional Specialist; ME = Municipal Engineer; O = Operation Officer/Procurement Specialist;

SE = Sanitation Engineer; UP = Urban Planner; WSE = Water Supply Engineer.

Other Project Data

Borrower/Executing Agency:

FOLLOW-ON OPERATIONS

<i>Operation</i>	<i>Loan no.</i>	<i>Amount (US\$ million)</i>	<i>Board date</i>
Surabaya Urban Development	3726	175.0	4/12/94
Semarang-Surakarta Urban Development	3749	174.0	6/7/94
Kalimantan Urban Development	3854	136.0	3/21/95
Second Sulawesi Urban Development	4105	155.0	11/21/96
Second East Java Urban Development	4017	142.7	5/16/96
Bali Urban Improvement	4155	110.0	5/6/97

Annex B. OED Project Evaluation Criteria

Definitions of Eight Key Criteria

1. Relevance Of Objectives

Definition: the extent to which the project's objectives are consistent with the country's current development priorities and with current Bank country and sectoral assistance strategies and corporate goals (expressed in PRSPs, CASs, SSPs, OPs)

Ratings

(i) **Each type of objective** will be rated as follows:

High	Project objectives of this type play a key role in the country's current development priorities and the Bank's current country assistance strategy, and are fully consistent with the Bank's current sectoral assistance strategy and corporate goals and policies
Substantial	Project objectives of this type are mostly consistent (minor shortcomings only) with the country's current development priorities, the Bank's current country and sectoral assistance strategies, and the Bank's current corporate goals and policies
Modest	Project objectives of this type have one or more significant inconsistencies with the country's current development priorities, the Bank's current country and sectoral assistance strategies, or the Bank's current corporate goals and policies
Negligible	Project objectives of this type are mostly inconsistent with, and possibly counterproductive to, the country's current development priorities, the Bank's current country and sectoral assistance strategies, or the Bank's current corporate goals and policies

(ii) **Overall relevance** will be rated as follows:

High	Most of the major objectives were highly relevant
Substantial	Most of the major objectives were at least substantially relevant
Modest	Most of the major objectives were not highly or substantially relevant
Negligible	Most of the major objectives were irrelevant or negligibly relevant

2. Efficacy

Definition: the extent to which the project's objectives were achieved, or expected to be achieved, taking into account their relative importance

Ratings

(i) **Each type of objective** will be rated as follows:

High	Objectives of this type were fully met, or expected to be fully met, with no shortcomings
Substantial	Objectives of this type generally were met, or expected to be met, with only minor shortcomings
Modest	Objectives of this type were met, or expected to be met, but with significant shortcomings
Negligible	Objectives of this type were not met, or expected not to be met, due to major shortcomings

(ii) **Overall efficacy** will be rated as follows:

High	Major objectives were fully met, or expected to be fully met, with no shortcomings
Substantial	Major objectives were met, or expected to be met, with only minor shortcomings
Modest	Major objectives were met, or expected to be met, but with significant shortcomings
Negligible	Most objectives were not met, or expected not to be met, due to major shortcomings

3. Efficiency

Definition: *the extent to which the project achieved, or is expected to achieve, a return higher than the opportunity cost of capital and benefits at least cost compared to alternatives*

Ratings

High	Project represents sector/industry best practice in terms of cost effectiveness, and economic returns (if estimates are available) greatly exceed the opportunity cost of capital
Substantial	Project meets sector/industry standards in terms of cost effectiveness, and economic returns (if estimates are available) exceed the opportunity cost of capital
Modest	Project fails to meet sector/industry standards in terms of cost effectiveness, and economic returns (if estimates are available) are near the opportunity cost of capital
Negligible	Project is well below sector/industry standards in terms of cost effectiveness, and economic returns (if estimates are available) are significantly below the opportunity cost of capital

4. Sustainability

Definition: *the resilience to risk of net benefits flows over time. Assessments of sustainability take into account nine factors, including technical, financial, and economic:*

- **Technical resilience**
- **Financial resilience** (including policies on cost recovery)

- **Economic resilience**
- **Social support** (including conditions subject to Safeguard Policies)
- **Environmental resilience**
- **Government ownership** (including by central governments and agencies, and availability of O&M funds)
- **Other stakeholder ownership** (including local participation, beneficiary incentives, civil society/NGOs, private sector)
- **Institutional support** (including supportive legal/regulatory framework, and organizational and management effectiveness)
- **Resilience to exogenous influences** (including terms of trade, economic shocks, regional political and security situations)

Ratings

(i) **Each factor** will be rated as follows:

High	The factor clearly is currently met and highly likely to continue, contributing to sustainability of net benefits
Substantial	The factor is currently met and likely to continue, contributing to sustainability of net benefits
Modest	The factor may currently be met, but it seems unlikely to continue, to the detriment of sustainability of net benefits
Negligible	The factor is currently not met and is highly unlikely to be met, to the detriment of sustainability of net benefits

(ii) **Overall sustainability** will be rated as follows:

Highly Likely	Project net benefits flow meets most of the relevant factors determining overall resilience at the “high level”, with all others rated at the “substantial” level
Likely	Project net benefits flow meets all relevant factors determining overall resilience at the “substantial” level
Unlikely	Project net benefits flow meets some but not all relevant factors determining overall resilience at the “substantial” level
Highly Unlikely	Project net benefits flow meets few of the relevant factors determining overall resilience at the “substantial” level
Not Evaluable	Insufficient information available to make a judgment

5. Institutional Development Impact (IDI)

Definition: *the extent to which a project improves the ability of a country or region to make more efficient, equitable and sustainable use of its human, financial, and natural resources through: (a) better definition, stability, transparency, enforceability, and predictability of institutional arrangements and/or (b) better alignment of the mission and capacity of an organization with its mandate, which derives from these institutional arrangements. IDI includes both intended and unintended effects of a project.*

Ratings

(i) **Each objective type** will be rated as follows:

High	Project objectives of this type made, or are expected to make, a critical contribution to the country's/region's ability to effectively use human, financial, and natural resources
Substantial	Project objectives of this type made, or are expected to make, a significant contribution to the country's/region's ability to effectively use human, financial, and natural resources
Modest	Project objectives of this type increased, or are expected to increase, to a limited extent the country's/region's ability to effectively use human, financial, and natural resources
Negligible	Project objectives of this type made, or are expected to make, little or no contribution to the country's/region's ability to effectively use human, financial, and natural resources

(ii) **Overall institutional development impact** will be rated as follows:

High	Project as a whole made, or is expected to make, a critical contribution to the country's/region's ability to effectively use human, financial, and natural resources, either through the achievement of the project's stated ID objectives or through unintended effects
Substantial	Project as a whole made, or is expected to make, a significant contribution to the country's/region's ability to effectively use human, financial, and natural resources, either through the achievement of the project's stated ID objectives or through unintended effects
Modest	Project as a whole increased, or is expected to increase, to a limited extent the country's/region's ability to effectively use human, financial, and natural resources, either through the achievement of the project's stated ID objectives or through unintended effects
Negligible	Project as a whole made, or is expected to make, little or no contribution to the country's/region's ability to effectively use human, financial, and natural resources, either through the achievement of the project's stated ID objectives or through unintended effects

6. Outcome

Definition: *the extent to which the project's major relevant objectives were achieved, or are expected to be achieved, efficiently.* The outcome criterion takes into account **relevance** at the time of the evaluation: whether the operation's objectives are consistent with the country's current development priorities and with current Bank country and sectoral assistance strategies and corporate goals; **efficacy**: whether the operation is expected to achieve its stated goals; and **efficiency**: the relation of results to costs.

Ratings

Highly Satisfactory	Project achieved or exceeded, or is expected to achieve or exceed, all its major relevant objectives efficiently without major shortcomings
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Satisfactory	Project achieved, or is expected to achieve, most of its major relevant objectives efficiently with only minor shortcomings
Moderately Satisfactory	Project achieved, or is expected to achieve, most of its major relevant objectives efficiently but with either significant shortcomings or modest overall relevance
Moderately Unsatisfactory	Project is expected to achieve its major relevant objectives with major shortcomings or is expected to achieve only some of its major relevant objectives, yet achieve positive efficiency
Unsatisfactory	Project has failed to achieve, and is not expected to achieve, most of its major relevant objectives with only minor development benefits
Highly Unsatisfactory	Project has failed to achieve, and is not expected to achieve, any of its major relevant objectives with no worthwhile development benefits

7. Bank Performance

Definition: *the extent to which services provided by the Bank ensured quality at entry and supported implementation through appropriate supervision (including ensuring adequate transition arrangements for regular operation of the project)*

Ratings

Highly Satisfactory	Bank performance was rated as Highly Satisfactory on both quality at entry and supervision, or Highly Satisfactory on the one dimension with significantly higher impact on project performance and at least Satisfactory on the other
Satisfactory	Bank performance was rated at least Satisfactory on both quality at entry and supervision, or Satisfactory on the one dimension with significantly higher impact on project performance and no less than Unsatisfactory on the other
Unsatisfactory	Bank performance was not rated at least Satisfactory on both quality at entry and supervision, or Unsatisfactory on the one dimension with significantly higher impact on project performance and no higher than Satisfactory on the other
Highly Unsatisfactory	Bank performance was rated as Highly Unsatisfactory on both quality at entry and supervision, or Highly Unsatisfactory on the one dimension with significantly higher impact on project performance and no higher than Unsatisfactory on the other

8. Borrower Performance

Definition: *the extent to which the borrower assumed ownership and responsibility to ensure quality of preparation and implementation, and complied with covenants and agreements, towards the achievement of development objectives and sustainability*

Ratings

Highly Satisfactory	Borrower performance was rated Highly Satisfactory on at least two of the three performance factors
Satisfactory	Borrower performance was rated at least Satisfactory on two of the three factors
Unsatisfactory	Borrower performance was not rated at least Satisfactory on two of the three factors
Highly Unsatisfactory	Borrower performance was rated Highly Unsatisfactory on at least two of the three factors

Comments from the Borrower



DEPARTEMEN PERMUKIMAN DAN PRASARANA WILAYAH
DIREKTORAT JENDERAL TATA PERKOTAAN DAN TATA PERDESAAN
 Jalan Pattimura No. 20 Kebayoran Baru - Jakarta Telp. 021 - 7221772, Kode Pos 12110



Our : HL.02.01-DK/191

31 May 2001

Mr. Alain Barbu
 Manager Sector and Thematic Evaluation Division
 The World Bank
 1818 H Street N. W.
 Washington D. C. 20433
 U.S.A

**Subject: Comments on Performance Audit Report of East Java Bali
 UDP and Sulirja UDP.**

Dear Mr. Barbu,

Thank you for your letter submitting the above performance audit reports. After reviewing the report together with a group of persons who has been directly involved in the project, we are pleased to submit to you our following comments on the report:

General

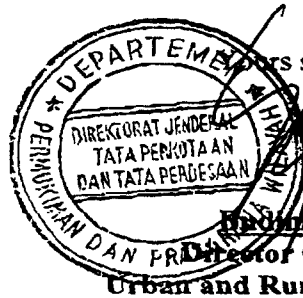
1. It seems to us that the reports were intended to provide a 'performance audit for two projects', but tended to express a conclusion that should in fact be analysed at the program rather than at the project level. We would like to suggest the Bank to undertake a 'program audit' in addition to the project performance audit.
2. We totally agree with the report that there was an overgeneralization in the treatment of diverse condition of the cities and regions in IUIDP. This is what the reform of the thinking in the current era wants to correct by allowing for more diverse solutions and differentiation based on local conditions. It should however be understood that past IUIDP was urged to implement the agenda on a broad based covering all over the Indonesian region to expedite distribution of the development and ensuring an equitable distribution of urban infrastructure and services. To be able to reach such a wide coverage program and implement the program very fast the government did not have any other choice than to standardize the approach, with consequences of the said shortcomings.
3. We have always argued against opinion that IUIDP or the 'urban approach' was too complicated or overly comprehensive and need to be simplified. It should be understood that urban management is always complicated and comprehensive. Such complexity and many sectors is the

characteristic of any urban development that any urban managers have to face. They cannot escape from that situation, or otherwise means they want to create a virtual city that is simple and consists of limited number of sectors or involving only a limited number of agencies, a wishful thinking of creating a world that only exist in imagination but never in real practice.

4. We have also argued against comparing Indonesia with conditions in other parts of the world since such comparison is futile and does not have any relevance. Every country has its own historical, cultural, political, economic, administrative, and environment background. So taking the Brazilian experience cannot have any relevance with Indonesia.
5. Although RIAP and LIDAP have been mentioned in the report unfortunately the report did not provide a critic on the reasons why implementation of the RIAP and LIDAP was not achieving the intended objectives of the action plans contained in the two important documents. We felt that management of UDP has to be improved to include a Project Implementation Unit (PIU) with equal mandate and intensity of monitoring as the physical elements of the Project. The report has in our view escape the attention of addressing the issue of the RIAP and LIDAP.

Specific Comments : (attached)

Thank you for your kind cooperation.

Yours sincerely

Endang Arif
 Director General of
 Urban and Rural Development

cc.

1. Mr. Keshav Varma Director Urban Development Sector Unit East Asia and Pacific Region The World Bank Washington.
2. Mr. Mark Baird Country Director Indonesia The World Bank RSI.

Comments from the Borrower



REPUBLIC OF INDONESIA
MINISTRY OF SETTLEMENTS AND REGIONAL INFRASTRUCTURE
Jl. Pattimura No. 20 Kebayoran Baru-Jakarta Selatan 12110 Tel. (62-21) 72796158, Fax. 72796155



Our Ref. : *HL.02.01-DK/210.*

15 June 2001

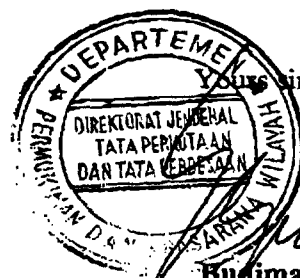
Mr. Alain Barbu
Manager,
Sector and Thematic Evaluations Group
Operations Evaluation Department (OED)
The World Bank
1818 Street N.W.
Washington D.C. 20433
U.S.A

**Re : Performance Audit Report for East Java Bali UDP and Sulawesi - Irian Jaya UDP
Comments on PAR**

Dear Mr. Barbu,

Further to our letter HL.02.01-DK/191 dated 31 May 2001, we have pleasure to enclose further comments to assist you in finalizing the PAR.

Thank you for your kind attention



Yours sincerely,

Budiman Arif

Director General of Urban and Rural Development

cc.:

1. Mr. Keshav Varma, Director Urban Development Sector Unit, East Asia and Pacific Region, The World Bank, Washington.
2. Mr. Mark Baird, Country Director Indonesia, The World Bank RSI.

**EAST JAVA BALI URBAN DEVELOPMENT PROJECT (LOAN 3304-IND) AND
SULAWESI IRIAN JAYA MUNICIPAL / URBAN DEVELOPMENT PROJECT
(LOAN 3340-IND)**

**GOI DETAILED COMMENTS ON PERFORMANCE AUDIT REPORT
(June 2001)**

A. GENERAL

- (i) In places, the report is colloquial and uses language that is difficult for non-native English speakers to understand.
- (ii) It is suggested that the report is reproduced using standard Bank formats with paragraph numbering. In these comments, we have manually numbered the paragraphs commencing with the preface. For example, paragraph 24 at the foot of page 7 starts with "Financial capacity was also uneven".
- (iii) The report should be rewritten, avoiding expressions like "the first baby gets a lot of attention" (para 19) or "People needed more handholding than the Bank could provide." in paragraph 46. Paragraph 48, 55 and 60 should be revised for similar reasons.
- (iv) From the text, the reader has the impression that the project outcomes have been better in East Java / Bali (with noted exceptions) compared to Sulawesi / Irian Jaya. In contrast, the Audit gives the same ratings for each of the 5 evaluation criteria.

B. PREFACE

- (i) GOI has no comments

C. BACKGROUND

- (i) Para 17. For logistical reasons, EJB consultants were based close to project locations with consequential better assignments results. In contrast, the distances involved in preparing, designing and supervising SIJ sub-project components had a negative impact on achieving the targeted outputs. It is also meant there was less time for consultation with local government personnel who, due to lack of training and UDP exposure, were less able to contribute than some of their counterparts in EJB. It is not automatically the case that senior consultants prefer to work outside of SIJ. It is also not correct that these consultants are "less professional".
- (ii) Para 19. The expression "traditional connections with central government" should be deleted because the IUIDP effort treated every region equally. GOI gave the same attention to SIJ, and this is borne out by the fact that most local governments in these areas can manage their affairs at least as well as their counterparts in EJB. Delete the reference to the "first baby".
- (iii) Para 22. IUIDP has been applied throughout the country for a broad range of urban areas. It was never a package suited to a medium-sized city, and planners / designers have not experienced major difficulties in applying the IUIDP approach to any size of urban area. On the contrary, the program was infinitely more adaptable compared

to preceding sectoral projects in responding to local needs. This very important point is missing from the whole Performance Audit Report.

- (iv) Para 23. It is correct that many EJB local governments took the initiative to start IUIDP planning, but is not correct to imply that "plans needed only a bit of refinement by consultants". At that time, there were very comprehensive consultations between the local and provincial governments, supported by TA services contracted by DGCK, representing the first effort in promoting "bottom-up" planning in Indonesia (despite its limitations). The last sentence gives a negative impression. Throughout Indonesia, GOI representatives travelled to the regions to inform the local governments that the IUIDP approach would govern all future urban investments. This is equally true of EJB and SIJ, although once the benefits of the program were recognized, local government responses have been reasonably consistent and favourable.

D. IMPLEMENTATION

- (i) Para 25. GOI does not agree that implementation did not address "the details of participating cities". As indicated above, all cities and towns were invited to participate in IUIDP program and the approaches adopted in each urban area reflected its size. GOI does not agree with OED that IUIDP was designed for generic medium sized cities.
- (ii) Para 26. The economic crisis started in July 1997 and did not start to have impact on regional budgets until 1998/99 by which time last disbursement had already taken place. The crisis is irrelevant in this PAR and all reference should therefore be deleted. The last sentence does not make sense; local investment plans (PJMs) were based as much as possible on local needs and priorities for the IUIDP sub-sectors. Optimizing the allocation of financial resources is considered a strong IUIDP attribute, whereas OED implies a criticism of this approach.
- (iii) Para 28. As already implied in paragraph 34 in SIJ, the East Java Bali RIAPs were not the sole cause of revenue improvements. Nevertheless, the effort certainly contributed to a greater awareness in local governments towards increasing local funding for urban infrastructure (see also section G below).
- (iv) Para 29. It is acknowledged that sectoral master plans were normally not available, but this should not imply that investment were not adequately planned and designed. Investments did tend to focus on short to medium term needs because these represented local priorities in response to the bottom-up planning techniques. The last sentence refers to the weak water supply agenda. It must be remembered that at the time of project preparation, many water supply projects were only just being completed under existing donor funded projects (eg. 2nd East Java Water Supply Project) and therefore the need for new investments was not a high priority. It should also be remembered that water enterprises in many regions were in the process of transfer to the local governments (i.e. new PDAMs). It would be helpful if OED recognized these conditions in the PAR in order to draw a more balanced judgement of the projects' achievements.

- (v) Para 32. Examples of unintended negative environmental impacts should be provided. If necessary, OED should provide an Annex describing the negative impacts observed by its auditors.
- (vi) Para 33. The apparent weaknesses in the water sector are a result of the IUIDP approach, and the Government's objective of promoting multi-sectoral solutions in the targeted urban areas. There were two important factors: (i) EJB preparation took place while the sectoral 2nd EJWSP was still on-going, and (ii) it has taken time to inculcate the local governments that water supply investments (and also other municipal services) would be financed at the local level through own resource and subsidiary lending arrangements.
- (vii) Para 33 (also). The Performance Oriented Maintenance Management System (POMMS) was not successful because local governments were not ready to respond to this important IUIDP initiative. Also, it is questionable whether the system, if applied today 10 years later, would achieve any better performance. The whole concept of asset management in Indonesia is difficult to promote through a donor funded project; it should instead be a process of learning what is, in reality, just common sense. If facilities are required by the community / customer, then the service provider will have to undertake adequate O & M.
- (viii) Para 33 (also). From DGCK's experience, the participation of local government personnel in all stages of the project depended on the willingness to participate in the program, and also the ability of personnel assigned. GOI cannot accept the OED statement that "consultants ended up doing all the work."
- (ix) Para 33 (also). The septage treatment plant in Denpasar is functioning well in accordance with original investment objectives and designs.
- (x) Para 33 (also). Corrected table attached shows that the number of SAR planned property connections was exceeded.
- (xi) Para 34 (also). It is acknowledged that the decentralization objective in SIJ were too ambitious, but OED should recognize that IUIDP was the vanguard of "decentralization in action" long before the recent legislation. It must also be remembered that all regions in Indonesia had to be treated equally, and it would have been politically and institutionally impossible to promote different agenda in different regions.
- (xii) Para 35. GOI does not accept these conclusions. At all times, the local governments were invited to participate in the preparation of the project (both EJB and SIJ). The fact that some local governments were not active participants, or failed to field suitably qualified personnel, was not the fault of the project or DGCK. The lack of ownership was due to the local government's role in project development - active regions obviously benefited more than the less interested local governments. It is not true to say that PJMs were prepared in a hurry; the process of project preparation at all stages was conducted through maximum possible consultation and participation. For EJB, the PAR should refer to the phased preparation effort (i.e. project preparation was done for selected local governments, and other Batches were gradually introduced during the 1st two years of implementation). It must also be noted that in East Java, the need to deal with 36 local governments presented the

central and provincial governments with a much larger logistical and communications constraint than the 9 local governments in Bali.

- (xiii) Para 35 (also). The OED statement that there was "little integration at the local level" is not true, and is rejected by GOI. The selection of consultants by central government was a necessity at the time; this did not (and still does not) have any impact on the lack of integration. Again, the OED statement is not true and it is rejected by GOI. It is true that provincial and local governments would have preferred to engage their own consultants, but the local capacity to do so was absent, and donor funding would have been impossible (poorly qualified local firms and inadequate procurement capability to accord with Bank's guidelines).
- (xiv) Para 35 (also). Plans were in part a central government product (by definition) because they related only to public works affairs in urban areas. The reason for not adopting a broader approach is given in item (xxi) below. Also, as a rule, all investment plans were accompanied by comprehensive financing plans, so the observation of one BAPPEDA official should not be treated as a norm, but as an exception.
- (xv) Para 35 (also). OED may be referring to an isolated case. Actually (and this is an indisputable fact), considerable efforts were made to survey "real demands" for water during IUIDP preparation because the top down planning experience (the "numbers approach") under 2nd EJWSP for example was known at that time to be non-responsive to local needs. The OED statement is not correct if applied to the overall EJB and SIJ planning efforts in the water supply sector, and it cannot be accepted by GOI in its present form
- (xvi) Para 36. This is a sweeping observation. As observed above, some local governments participated actively, whilst others took more time to realize the benefits of IUIDP. All local governments were given equal opportunity to participate. It is accepted that some central government appointed consultants may not have had "an accurate sense of what the communities really wanted or needed", but GOI does not accept that this as a general picture. DGCK recalls extensive involvement of local governments in deciding drainage priorities to reduce flooding in urban areas, especially the urban poor communities. In contrast, investments in solid waste collection and transportation were determined with local governments and understandably, did not involve extensive community consultation except for new final and temporary disposal sites. The program's approach to determining water supply needs is described in item (xv) above.
- (xvii) Para 37. GOI welcomes the conclusions drawn by OED, but this should not focus on "attitudinal change". There were numerous other changes that took place, notably introducing benefit analysis to justify sub-project selection and better standards of construction compared to previous grant funded projects (under the Ministry of Home Affairs). By far the most rewarding aspect of the participation of local government personnel was the enthusiasm of many younger and newly qualified staff who otherwise lacked the opportunity to progress. Many of these personnel are now "middle weight" local government officers who are better prepared to handle the challenges now faced by the newly autonomous regions.

- (xviii) Para 38. GOI knew from the outset that competent local master plans did not exist for all sub-sectors in every targeted urban area. Consciously, GOI proceeded cautiously with IUIDP promoting a range of small to medium sized investments that could be managed by the respective local governments. To solve the issue presented by one involved Bank staff would have resulted in many planning reports, probably with a very wide range of technical competence, and also of dubious value. Such an approach would have taken an enormous effort which, by the time it was completed, would probably have resulted in a need to redo much of the planning documentation. At the time, GOI was also conscious of the relatively weak capability of local governments to execute such planning documents, and shared this view with the Bank.

- (xix) Para 39. GOI does not accept the observations of municipal staff that met with the audit mission. All sub-sector investments were, without exception, pre-planned in the PJMs and signed off by each local government. Again, DGCK repeats the above stated observation that those LGs that worked comprehensively and seriously in the preparation and implementation of IUIDP received the most benefit. Those that were tardy tended to be the complainants. The cited examples of pumps installed later than the pipelines was not a consequence of poor planning; nor was it common. It was a result of the project procurement arrangements that were agreed between GOI and the Bank at the time, and which are still applied today for all urban development project, whether or not these follow the IUIDP approach.

- (xx) Para 39 (also). The example of the sewage treatment plant without a water (GOI assumes that OED means "sewage") connection should be described more fully in an annex, with reasons presented to explain why this sub-project has not been successful. This can then serve as an example for future planners in the sanitation sector, and it would avoid the damning of the IUIDP approach because of one example. The problem of newly laid roads being damaged by pipelaying is not unique to Indonesia or IUIDP projects. Some local governments have infrastructure committees to coordinate installation of services (including power cables, telephone conduits, gas and water pipes), but even these are powerless if investment plans have already been made and budgets have been approved. IUIDP could not possibly have orchestrated all these issues, and it was never intended that it should (despite misplaced views in some local governments that this was the meaning of the term "integrated").

- (xxi) Para 40. From the outset, GOI recognized that the health and education sectors were not represented in IUIDP. It was already sufficiently difficult to mobilize the public works sector to respond to the need to decentralize its affairs in the provision of urban infrastructure. To have involved other technical departments at the time EJB and SIJ (and other IUIDPs) were formulated would have been IMPOSSIBLE. Furthermore, the local governments were not prepared and it is to be noted that decentralization of these other sectors (including transportation) is only now taking place following the effectiveness of Law 22/1999 on 1 January 2001. As already observed, DGCK with the support of the Bank were the vanguard of "decentralization in action". Since that is now happening throughout Indonesia, the sustainability of IUIDP in EJB, SIJ and all subsequent urban development projects should be considered as an unparalleled success.

- (xxii) Para 40 (also). The problems of unregulated housing built on hillsides in Irian Jaya is known by central and local governments. It was never intended to solve this problem under SIJ, and it should not be introduced into the PAR. Perhaps the Bank should help MSRI to support a resolution to this problem through the proposed settlements improvement program (previously HSL). In the same paragraph, GOI notes the lack of maintenance by local governments, and is equally disappointed.
- (xxiii) Para 41. For OED's information, the Kintamani water supply system has now resumed operations under a community agreement with the PDAM that was brokered with MSRI support. This was a very special problem that has occurred since the economic crisis because of the very high cost of pumping water to this mountain top community. It should therefore not be presented as typical of EJB performance.
- (xxiv) Para 55. The whole of this paragraph is not based on factual evidence, and it is unacceptable to GOI. The PAR should avoid simplistic statements of the type given in line 10. Many of the water enterprise problems existed before EJB and SIJ, and still persist; even so, the cost recovery criteria adopted under IUIDP is now recognized by local governments (even though this is made more complicated following the 1997/8 economic crisis).
- (xxv) Para 57. The issue of lack of local ownership has already been addressed above. The problem of funding source is acknowledged because it was necessary to secure central government counterpart budgets each year. This constraint applied to all projects (IUIDP and non-IUIDP) and persists today because of the fiscal transfer uncertainties following effectiveness of Law 25/1999. Budgeting problems also occurred at the local level, and for this reason the PJMs were dynamic so that they did respond to local conditions and available budgets.
- (xxvi) Para 57 (also). Many KIP projects were cancelled or substituted for reasons given in the PAR, demonstrating that the PJM was a flexible tool. The reference to "a perverse incentive for cities to plan several small and somewhat ad hoc projects" is not understood. OED is requested to clarify.
- (xxvii) Para 58. More should be made of this positive response from government officials to help balance many of the negative features in the PAR. Are these central, provincial and local officials, and in what direction should we build - more of the same; a broader IUIDP covering more sectors; how to approach the water supply and sanitation sub-sectors.
- (xxviii) Para 59. OED is requested to clarify what is meant by "perverse incentives". We are all well aware of the lack of professionalism in water system management. Significant improvements are bound to take time and this could not be expected of EJB and SIJ, the 1st 5-year IUIDP. Even now, after completion of a number of urban development projects, issues such as these continue to affect this sub-sector. For this reason, comprehensive reform measures are being proposed by central government. However, EJB and SIJ did strongly support the devolution of sub-sector responsibility to the regions and this should be recorded as a significant achievement.

- (xxix) Para 59 (also). GOI assesses that sanitation improvements under IUIDP generally, and under EJB and SIJ have been disappointing. Despite best efforts by DGCK to promote more attention to issues that affect community health and urban environments, it is a fact that local governments attached low importance to this sub-sector. The picture remains the same today despite a number of urban development projects implemented with the support of donor agencies, including the Bank. Lastly under this paragraph, the impact of the economic crisis on the project benefits could not have been foreseen (even by the Bank whose 1997 Country Report has to be changed prior to publication). GOI is of the opinion that this factor should not be applied in determining the projects' performance ratings.
- (xxx) Para 60. Efforts have been made in the Ministry of Home Affairs to broaden and deepen the scope of the PJM planning tool (referred to as....). MSRI is of the opinion that this is the correct trend, although it is recognized that its implementation following the enactment of the decentralization laws is difficult in the present political climate. However, what this does mean is that a system of local-centre planning is required and that _____ (or IUIDP version 3) can be considered as the embryo of a more comprehensive system that local governments will have to employ in the near future. EJB and SIJ and subsequent UDPs will have been the testing ground for such an approach. At the very least, lessons learnt will be used to ensure future planning tools are based on IUIDP experience. GOI would therefore rate the approach as likely to be sustainable but in a improved modified form.
- (xxxi) Para 60 (also). OED is referring to the "longer-term planning exercises", whereas paragraphs 29 and 38 have implied that there were no such planning tools available for EJB and SIJ. It can be concluded that the PAR is inconsistent in its assembly of statements from project participants / observers.
- (xxxii) Para 61. The PAR gives a better impression of both follow-on projects EJUDP II and SUDP II, indicating that lessons learnt from the 1st projects have been adopted. It is GOI's opinion that this fact illustrates sustainability of the programmatic approach that is fundamental to IUIDP.
- (xxxiii) Para 61 (also). It is acknowledged that the follow-on projects have been prepared more rigorously. This is a direct consequence of the approaches developed during EJB and SIJ where sub-project components in the latter years came under greater scrutiny.
- (xxxiv) Para 62. It is GOI's opinion that the majority of the EJB and SIJ sub-project components are important infrastructure assets that will continue to serve the urban communities. As already observed above, the programmatic approach has been continued into follow-on projects, and is likely to be adopted for similar donor funded urban development programs and as a routine GOI planning and programming technique. For these reasons, sustainability is likely but in a modified form based on lessons learnt.
- (xxxv) Para 64. GOI rates the Bank's performance very highly because of the detailed attention given to the numerous problems that emerged during IUIDP start-up. GOI does not believe that O & M was a debacle, but it does share the view that POMMs

and other asset management tools are extremely difficult to apply in a local government environment that was not (and is still not) highly motivated.

- (xxxvi) Para 65. As indicated in item (iv) above, SIJ probably did not perform as well as EJB. However, the PAR ranks the outcome of both projects the same.
- (xxxvii) Para 67. GOI notes that the Bank's performance is upgraded to satisfactory compared with the ICR. However, despite the reasons presented, it is GOI's view that the Bank's performance in EJB was better than SIJ, and this should be reflected in the Principal Ratings on page 2 of the PAR.
- (xxxviii) Para 69. This paragraph should be reworded avoiding expressions like "its cookie-cutter approach" which is not understood. It has also been argued above that IUIDP is not suited only to medium-size cities. The last 4 sentences are only stating the obvious, and have not been discussed in the main body of the PAR - so they are not conclusions or lessons.
- (xxxix) Para 70. GOI agrees with these conclusions except the reference to smaller towns and cities. IUIDP is an important stepping stone for decentralization, and it does support the development of regional autonomy. As a planning and programming tool it should be seen as the embryo of a broader based annual programming activity by all local governments that embraces all activities in these regions and embracing both urban and rural areas. This was (and still is) the philosophy behind the East Java Strategic Regional Development Program (see Abbreviations and Acronyms). There is no doubt that this is the approach to follow for a developing nation that needs to marshall its development budgets in an optimal and well-focussed manner. Without IUIDP, this level of awareness in the regions would be absent and the present laws on decentralization would be even more difficult to implement.
- (xli) Para 74. GOI is not convinced that there was a lack of parallel efforts in solid waste management and drainage improvements. This problems stems from both a lack of facilities and also community habits that will take many years to change; certainly such an objective could not be achieved in a 5-year time frame of a multi-dimensional program such as IUIDP. As the Bank is aware, Indonesia's cultural, political, economic, administrative and environmental backgrounds are unique, so that direct comparison with projects in Brazil is not relevant.
- (xlii) Para 75. GOI believes that the institutional support for cost recoverable sub-sectors have been handled in a correct manner, and was different from the non-revenue generating activities. It is agreed that more effort is required to achieve cost recovery, but the Bank is well aware of the enormous constraints faced, for example, in the water supply sector.
- (xliii) Para 76. The rolling planning process should be sustainable. Unfortunately the PJM is seen by many as a tool to promote a donor funded UDP. The need to institutionalize such an approach is considered essential, and would require a unique cooperative effort between the main central government actors, especially Bappenas, MoHARA, MoF and MSRI and the Coordinating Ministry for the Economy.
- (xliv) Para 77. This statement is not relevant to the performance audit.

- (xliv) Para 78. The PAR is proposing the impractical. TA management was already sufficiently complex, and it is unlikely that these suggestions could have worked for EJB / SIJ and nor could they work now.

(page 23) Other Project Data. The BUIP loan number is 4155

E. OTHER ISSUES

- (a) The PAR does not mention the slow procurement of consultant support by central government, and the consequences felt in the regions, because provincial and local governments did need these services in order to respond to the program objectives.
- (b) There is only a brief mention of the change from grant assisted projects to a program that was based on a mixture of grant support, local funding, own revenues and subsidiary lending. In itself, this was a major departure from tradition, and both EJB and SIJ contributed very strongly towards this essential objective for future development programs. It is worth noting that initially this approach often met with a hostile reception, and many parties tried to maintain the *status quo* which was by then unsustainable.