

**REPORT AND RECOMMENDATION
OF THE
PRESIDENT
TO THE
BOARD OF DIRECTORS
ON A
PROPOSED LOAN
TO THE
ISLAMIC REPUBLIC OF PAKISTAN
FOR THE
NORTH-WEST FRONTIER PROVINCE
URBAN DEVELOPMENT SECTOR PROJECT**

October 2001

CURRENCY EQUIVALENTS

(as of 14 October 2001)

Currency Unit	–	Pakistan Rupee/s (PRs/PRs)
PRs1.00	=	\$0.01210
\$1.00	=	PRs82.6255

Pakistan maintains a market-based exchange rate system. For the purpose of calculations in this report, an exchange rate of PRs51.50 = \$1.00 has been used. This was the rate prevailing at the time of appraisal.

ABBREVIATIONS

ADB	–	Asian Development Bank
BME	–	benefit monitoring and evaluation
CBO	–	community-based organization
DOF	–	Department of Finance
EIRR	–	economic internal rate of return
FIRR	–	financial internal rate of return
IEE	–	initial environmental examination
LGGERD	–	Local Government, Elections and Rural Development
MC	–	municipal committee
MOF	–	Ministry of Finance
NGO	–	nongovernment organization
NWFP	–	North-West Frontier Province
O&M	–	operation and maintenance
PCU	–	project coordination unit
PDD	–	Planning and Development Department
PIT	–	project implementation team
PPHD	–	Physical Planning and Housing Department
PUDB	–	Provincial Urban Development Board
SUDP	–	Second Urban Development Project
TA	–	technical assistance
WSD	–	Works and Services Department

NOTES

- (i) The fiscal year (FY) of the Government ends on 30 June.
- (ii) In this report, "\$" refers to US dollars.

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LOAN AND PROJECT SUMMARY

Borrower	Islamic Republic of Pakistan
Project Description	<p>The Project will help improve urban infrastructure in up to 24 urban centers within North-West Frontier Province (NWFP). The urban centers have major deficiencies in infrastructure and delivery of services in subsectors given high priority by the provincial government under its Provincial Spatial Development Framework and Strategy and sector investment needs program. The Project also aims to improve the capacity of local governments to provide, operate, and maintain essential urban services in line with the Government's devolution program.</p>
Classification	Primary: Pro-poor growth Secondary: Human development
Environmental Assessment	Category B An initial environmental examination was undertaken.
Rationale	<p>Urban centers in the NWFP are experiencing rapid growth and rising demand for improved urban services. Current deficiencies in basic infrastructure are inhibiting human development and economic growth, and severely constraining the potential for urban areas to play a more significant role in economic growth of the province. The Government's proposed devolution policy will place new demands on local governments to improve financial and institutional capacity and human resource management.</p> <p>NWFP's Urban Investment Plan, together with the Government's poverty reduction initiatives and greater devolution of power and responsibility to local governments to provide and finance urban infrastructure and municipal services, all require support. Participatory approaches need to be developed together with (i) institutional development and devolution of service delivery; (ii) targeting of low-income communities; (iii) financial equity and cost recovery at the local government level; (iv) partnerships between communities and local governments; (v) priority investments in basic services that will impact on the lives of low-income groups; and (vi) stimulation of demand-driven competition.</p>
Objectives and Scope	<p>The main aim of the Project is to support the (i) devolution of responsibility and authority to local governments by expediting the policy reform process in the sector, (ii) decentralization of economic growth to reduce provincewide disparities, and (iii) reduction of urban infrastructure deficiencies. The specific objectives are to (i) demonstrate effective interventions in urban service management that can be replicated, (ii) stimulate a</p>

progressive shift of responsibilities to urban local governments for financing and management of urban services, and (iii) improve management and resource mobilization capacities of urban local government.

The Project will finance high-priority basic infrastructure investment in accordance with the needs of each participating municipal committee (MC), in the context of their medium-term investment needs. Infrastructure will consist of subprojects in water supply, sewerage and sanitation, drainage, solid waste management, and roads and local access. The Project will consist of two components: (i) urban development, including infrastructure improvements and community development and participation; and (ii) institutional development, including project implementation support, municipal finance capacity building, and incremental administrative support.

Cost Estimates

The Project cost is estimated at \$30.0 million equivalent, of which \$8.7 million equivalent is the foreign exchange cost and \$21.3 million equivalent the local currency cost.

Financing Plan

Source	(\$ million)			
	Foreign Exchange	Local Currency	Total Costs	Percent
ADB	8.5	12.3	20.8	69
NWFP	0.2	7.2	7.4	25
MCs	0.0	1.8	1.8	6
Total	8.7	21.3	30.0	100

ADB = Asian Development Bank, MC = Municipal Communities, NWFP = North-West Frontier Province.

Loan Amount and Terms

A loan of SDR 16,136,000 (\$20.8 million equivalent) will be provided in various currencies from the Asian Development Bank's (ADB) Special Funds resources for a term of 32 years, including a grace period of 8 years, and with an interest rate of 1 percent per annum during the grace period and 1.5 percent per annum thereafter.

Relending Terms

The MCs will be required to finance the incremental administration costs associated with their investments in the Project, and a minimum of 20 percent of the cost of capital works of town-specific subproject costs, increasing to a maximum of 50 percent based on the MCs current and projected financial capacity at the time of subproject approval, through subloans using project funds. Tripartite subsidiary project agreements, including grant and subloan components, will be entered into between the NWFP Department of Finance, Local Government, Elections and Rural Development (LGERD), and the participating MCs. Subloans to the MCs will be at an interest rate of 7 percent per annum, with a grace period of three years and repayment of principal over 12 years. The subsidiary

project agreements will include standard terms and conditions, and will be supported by a loan agreement between the NWFP Department of Finance and the Ministry of Finance.

Period of Utilization

Until 30 June 2008

Executing Agency

The Executing Agency for the Project will be the NWFP government through LGERD.

Implementation Arrangements

A project steering committee to oversee the Project, and to be chaired by secretary, LGERD, with committee members representing Department of Finance, Planning and Development Department, Works and Services Department, and the departments handling the functions of the Physical Planning and Housing Department, Public Health Engineering Department and environmental concerns, will meet at least twice a year and as often as required. A project coordination unit (PCU) will be established in LGERD, and will (i) prepare the overall project implementation plan and the consolidated annual work plan, (ii) coordinate and appraise subproject feasibility studies, (iii) provide technical support and supervision functions for subproject implementation, (iv) plan and coordinate activities to improve local government financial management, (v) plan and guide community participation, (vi) provide advice on terms of reference and consultant selection for design and supervision of subprojects, (vii) facilitate project coordination, (viii) prepare consolidated progress reports and documentation, (ix) organize benefit monitoring and evaluation activities, and (x) prepare the project completion report. The PCU will be headed by a project director from LGERD. The PCU's agenda of activities range from the continual monitoring of MC participation criteria to the screening and development of the physical investment program. The PCU will provide technical support and supervisory functions for subproject implementation, and have 12 professional staff, supported by international and domestic consultants.

Procurement

Procurement will generally be carried out by the MCs under the guidance of the PCU. All procurement will follow ADB's *Guidelines for Procurement*. Since most of the project sites will be small and scattered, the Project will not likely attract international civil works contractors. All subprojects are expected to cost less than \$1.0 million and will therefore be undertaken through local competitive bidding in accordance with procedures acceptable to ADB. Where the contract value exceeds \$1.0 million, the contract will be procured through international competitive bidding procedures. Equipment items that are locally available and cost more than \$50,000 equivalent and less than \$100,000 equivalent may be procured through local

competitive bidding, while items costing less than \$50,000 may be procured through direct purchase in accordance with procedures acceptable to ADB. International shopping will be followed for materials and equipment packages estimated to cost more than \$100,000 but less than \$500,000 equivalent, while for materials and equipment packages costing in excess of \$500,000 equivalent, international competitive bidding will be used. All procurement will be channeled through the PCU for concurrence before submission to ADB for approval.

Consulting Services

To support project implementation, a total of 396 person-months of consulting services (36 person-months international and 360 person-months domestic) will be required, covering (i) project management support to the PCU and project implementation teams, including subproject preparation and appraisal, and capacity building for subproject implementation by local government agencies (214 person-months); and (ii) capacity building for municipal financial management to the MCs, to improve accounting systems and increase local revenues (182 person-months). Consultants will support LGERD and MC staff. The consultants will be engaged through a firm under a single contract, and in accordance with ADB's *Guidelines on the Use of Consultants* and other arrangements satisfactory to ADB on the engagement of domestic consultants. In addition, one or more NWFP-based nongovernment organizations, to be recruited by a government committee, in accordance with established guidelines, will be involved in the process of establishing sustainable government-community partnerships, for the development of effective and lasting channels of communication.

Estimated Project Completion Date

31 December 2007

Project Benefits and Beneficiaries

The Project will improve the living conditions of about 400,000 residents in up to 24 urban centers, by enhancing the quality of life and health, improving the environment, and creating conditions conducive to sustained urban development and economic growth. The Project will contribute to reduced mortality, morbidity, and poverty, and the loss of amenity associated with environmental degradation in urban centers, especially among slum inhabitants and poor groups, particularly women and children, who are estimated to make up 15 percent of the urban population. The Project will support improvements to local government capacity by improving their financial and operational management and planning, including local resource generation.



I. PROPOSAL

1. I submit for your approval the following Report and Recommendation on a proposed loan to the Islamic Republic of Pakistan for the North-West Frontier Province (NWFP) Urban Development Sector Project.

II. INTRODUCTION

2. The Government has recognized the need for greater responsibility and decision making by lower levels of government, especially within urban centers where high growth rates, combined with the slow development of the urban sector are resulting in uncontrolled and unplanned development. Recently the Government initiated a policy of devolution of responsibility for development to local governments and communities. The mobilization of local resources and improved management of existing urban infrastructure and services are paramount to achieving these objectives. To achieve this goal, the Government has requested Asian Development Bank (ADB) assistance in developing the economic potential of urban centers in NWFP by improving existing infrastructure, and developing the required institutional capacity of local governments. The Appraisal Mission¹ was undertaken from 14–23 June 2000. This report is based on the consultant's reports prepared during an ADB-financed technical assistance (TA),² and the Mission's understandings with both the federal and provincial governments, and with senior town officials and community groups. The linkage between the project objectives, inputs, and outputs are shown in the project framework in Appendix 1.

III. BACKGROUND

A. Sector Description

1. Trends and Conditions

3. Pakistan's population, estimated at 135 million in 1999, is growing at about 2.3 percent per annum. The urban population of about 47 million, estimated to be growing at 5 percent per annum, accounts for approximately 35 percent of the total. This high rate of urban growth is expected to continue in the foreseeable future, in view of the country's relatively high birth rate, migration from rural areas in search of employment, and industrial and commercial growth in urban centers. By 2020, the urban population is expected to almost triple to around 115 million, accounting for about 50 percent of the total population. The annual national per capita income is about \$483. The 1998 United Nation Development Programme human development index ranks Pakistan 138th among 174 countries and classifies it as a medium human development country. However, this ranking is lower than Pakistan's rank in real gross domestic product per capita, indicating that more emphasis should be placed on human development. The infant mortality rate is about 85 per 1,000 live births, and life expectancy is estimated at 63 years for men and 62 years for women. Despite significant progress during relatively high economic growth in the 1980s, poverty incidence remains high, with an estimated one quarter to one third of the population living below the poverty line.³

¹ The Mission comprised W. A. Costin, Sr. Urban Development Specialist and Mission Leader; V. S. Rekha, Counsel; and S. A. Khan, Sr. Project Implementation Officer, Pakistan Resident Mission. The Pakistan Resident Mission provided guidance and support to the Mission.

² TA 2940-PAK: *North-West Frontier Province Urban Development Project*, for \$1.15 million, approved on 12 December 1998.

³ Poverty is defined in terms of deprivation of a minimum bundle of the basic necessities of human life such as food, based on a consumption of 2,550 calories per day, clothing, and nonfood requirements.

4. High urban growth, combined with slow development of the urban sector, has resulted in uncontrolled and unplanned development of the cities and towns, deteriorating urban environment, and deficiencies in all forms of urban services, including water supply, sewerage, roads, drainage, and solid waste management. Lack of urban planning, land-use control, and construction regulations, coupled with limited skilled human resources and financial capacities, in almost all urban centers, has constrained the ability of governments to meet the overall needs of urban communities. Many slums have emerged in urban centers. NWFP is no exception to this phenomena. NWFP, with a total population of around 17 million, and an urban population of approximately 3 million, has an annual population growth rate of some 3.5 percent. In 1993/94 poverty incidence was estimated to be approximately 17.7 percent, with poverty incidence in urban areas accounting for around 15 percent. By 2020, the urban population in NWFP is expected to be 5.6 million. The current NWFP administrative boundary contains 7 divisions with 24 districts and 46 classified urban centers; populations in each range from a few thousand to a million in the capital city of Peshawar. Appendix 2 provides a list of the urban centers, their administration classification, population and growth rate, and per capita incomes as of 1998. Approximately half the towns in the province have populations ranging from 25,000 to 100,000. Average household size is 7.7 persons, with an average of 1.2 families per household.

5. Levels of urban services within NWFP urban centers can be generally characterized as low, especially in comparison with many other South Asian countries. Coverage and service levels vary greatly from town to town. While most of the towns have a water supply system, coverage of households with access to water supply ranges from 25 to 83 percent of the population. Due to lack of maintenance and poor initial construction, water losses in existing piped systems are in excess of 40 percent. Service levels in the sanitation sector are low; only four towns in the province have piped sewerage systems. However, a large percentage of households have individual sewage disposal systems, consisting mainly of pit latrines, and to a lesser extent, septic tanks. These systems are often in poor condition with overflows discharged into open canals and drainage networks, and infiltrating the surrounding groundwater aquifers. Drainage systems in the towns are dependent on open canals serving as both drainage and sewage collection points. Secondary and tertiary drainage systems are virtually nonexistent. While limited solid waste collection systems exist in most of the towns, waste is commonly disposed of in open fields and unsanitary dump sites. While urban road networks are reasonably extensive, they are all in extremely poor condition and maintenance is totally inadequate. Municipal facilities such as public markets, bus shelters, slaughterhouses, and community buildings are inadequate to meet the demands of the public. The existing standards and provision of urban infrastructure and services are generally insufficient to support sustained human development and economic growth in the urban centers.

2. Sector Institutions, Infrastructure, and Finance

a. Urban Sector Institutions

6. Responsibility for urban development and environmental management is distributed among various government organizations: local authorities, urban councils, cantonment boards, and departments handling public health engineering, communication and works. Details on the sector institutions are provided in Appendix 3. The NWFP Local Government Ordinance was promulgated in August 2001 and as many of the functions are being devolved from the provincial to the local government level, a number of government organizations are being reorganized and renamed. As many as 24 federal, provincial, and local government agencies are involved in urban development in NWFP. As a result, some functions, such as undertaking urban development projects, are duplicated by several agencies, while many other functions, such as urban planning, land-use control, construction regulation, and operation and maintenance (O&M) of completed urban facilities, are left without adequate attention. The

institutional framework through which urban areas are administered and developed is complex. Fundamental shortcomings are the separation of the budgeting role from the urban development planning role, and the absence of a clear framework for urban land-use planning. As a result, towns have no form of development control. In the absence of medium-term plans and budgets, the discontinuity created by perpetual political change prevents the realization of any urban development strategy.

7. Two main ministerial departments are largely responsible for the provincial institutional framework. The Local Government, Elections, and Rural Development Department (LGERD) is responsible for the administration of local councils. Originally exclusively responsible for local government administration, LCB has become increasingly involved in supporting local councils for planning, finance, and infrastructure engineering. The Physical Planning and Housing Department (PPHD) is the main department responsible for land-use planning, and guiding and controlling urban growth and development. The Provincial Urban Development Board within PPHD is a semiautonomous body, created to formulate policies on urban area development. Part of its powers are delegated to local area authorities, through the establishment of development authorities in the main urban centres (Dera Ismail Khan, Hazara, Kohat, Malakand, Mardan, and Peshawar). A separate project management unit headed by a director general was established under the Provincial Urban Development Board to implement the ADB-supported Second Urban Development Project (SUDP).⁴ The unit is also the counterpart agency for other urban development initiatives, in particular for the Community Infrastructure Project, an infrastructure upgrading project being implemented in 55 rural and urban low-income communities in NWFP and funded jointly by the World Bank, Swiss Agency for Development and Cooperation, and United Nations Children's Fund (UNICEF).

8. Central to all planning at the provincial level is the Planning and Development Department (PDD), headed by the additional chief secretary. It holds overall responsibility for planning and development of all NWFP sectors, including policy and procedures, and plays a key role by coordinating the preparation of annual budgets of the Provincial Annual Development Programme. In this capacity, PDD reviews investment proposals for development from all line departments, and prepares recommendations to the NWFP government, as part of the plan approval procedure. Most issues relevant to urban infrastructure fall under the responsibility of the additional secretary holding the PPHD portfolio.

9. Line departments are responsible for the delivery of major urban infrastructure projects. The Public Health Engineering Department is mandated to plan and construct water and sewerage works in urban areas. Once completed, water supply schemes are generally handed over to local councils. The Communication and Works Department is responsible for the construction, repair, and O&M of provincial roads (and associated roadside drains), bridges, and tunnels in the province. In many cases, to maintain sections of the national highway network, work is contracted by the National Highway Authority. Urban (local) roads are the responsibility of local councils, although this may also be subcontracted to the Communication and Works Department for practical purposes.

10. Urban local government⁵ in Pakistan is presently through local councils administered by LCB. Local councils currently include the Peshawar Municipal Corporation, 29 municipal

⁴ Loan 1004-PAK: *Second Urban Development*, for \$66.0 million, approved on 14 December 1989.

⁵ While the role and position of urban local government has changed due to the NWFP Local Government Ordinance promulgated in August 2001, with devolution of power to local governments, and the creation of district assemblies, the change will be more in terms of political form and financial autonomy than in administrative powers and function; laws, rules, and regulations will be amended as required.

committees (MCs),⁶ and 16 town committees. All towns under the proposed Project are classed as MCs. The MCs are grouped in categories, depending on the level of revenue, irrespective of the population size. LCB allocates staffing levels according to category, not to population size. The MCs are given a range of mandated functions. In addition to the provision of basic urban services and infrastructure, responsibilities include drawing up master plans and site development plans, and a form of building control. The MCs generally do not have adequate numbers of skilled staff or local revenue. Typical staff in an MC, depending on its size and covering administrative, financial, and engineering units, comprise an administrator, chief officer, various levels of clerks, accounts officer, accountant, tax officer, collectors, municipal engineer, subengineer, sanitary inspector, sanitary supervisor, and a number of sanitary workers. Maintenance of urban infrastructure is given low priority. Urban populations have little confidence in local government, and are reluctant to pay existing taxes and charges because of poor service delivery.

11. Planning legislation for local councils is included in the NWFP Local Government Ordinance (1979), which mandates the preparation of master plans. However, under the NWFP Urban Planning Ordinance (1978), the Provincial Urban Development Board, through its local area authorities, is delegated to prepare local area plans; this falls under a different provincial department. Current legislation does not recognize the concept of structure plans as a means to provide a medium-term framework for urban land-use planning that is immune to political change.

12. Elections for local councils were suspended in 1996, and towns are administered by an administrator appointed by the secretary, LGERD. The administrator is presently supported by officers heading four main departments. The main departments relevant to urban services and infrastructure are the (i) Health Department: responsible for sanitation (solid waste management, drainage, and vaccination); (ii) Water Supply Department: responsible for water supply, fire fighting, and street watering; and (iii) Building and Works Department: responsible for roads, general municipal works, building control, gardens, roadside drains, and street lighting.

b. Urban Infrastructure

13. Core areas of most urban towns suffer from inadequate infrastructure and poorly managed services. Town centers often lack adequate markets and other community facilities, and the number of low-income households living in slum and squatter settlements is steadily increasing. To meet growing pressures and demands, urban development has usually occurred with little or no effective environmental controls and with forms of urban governance that do not match the responsibilities. Little attention has been given to the environmental and social implications of such rapid urban expansion, including availability of water resources, job opportunities, human hygiene, social integration, and personal security and safety of the residents. Rapid urban expansion without effective governance means that in virtually every urban center a substantial proportion of the population is at risk from environmental, social, and economic threats. A survey undertaken by the TA consultants indicates that water supply, sanitation, and solid waste are the major concerns of town communities; road improvement and storm-water drainage are also highly ranked. While 37 percent of households have individual house connections to piped water systems, 2 percent rely on community standpipes, 37 percent on wells, and 24 percent on other sources. Problems concerning water supply generally relate to the lack of distribution systems and the quality and intermittent supply of water, often available less than six hours per day. The quality of drinking water is often low due to aging

⁶ Municipal Committees means a participating Tehsil Municipal Administration set up under the NWFP Local Government Ordinance, 2001, including any successor(s) thereof, functioning at the local government level of NWFP.

distribution systems, lack of local treatment facilities, and contaminated water sources in some urban centers. Sanitation facilities are generally insufficient with 40 percent of residents either connected to piped sewerage systems or dependent on individual septic tanks, with the remainder using pit latrines, bucket latrines, fields, or streams. Wastes from septic tanks and latrines are disposed of in drains and open areas, creating unhygienic conditions and contaminating the shallow water aquifers. The lack of treatment of wastewater and its direct disposal into waterways not only affects groundwater quality, but also depletes aquatic resources, and pollutes surrounding water bodies. Approximately 27 percent of solid waste is regularly collected by municipal authorities, with the waste being disposed of in open areas, without any proper treatment and protective measures. The remaining solid waste is disposed of by residents along roads and in open spaces and nearby water courses. No waste classification system exists, and hazardous waste is mixed with domestic waste. Town road networks are generally adequate but their condition, width, and quality of maintenance are inadequate. Drainage problems are often associated with poor flow conditions due to inadequate drain sizes and insufficient coverage. Stagnant water is common, causing health hazards and environmental degradation. Details of the existing infrastructure and services in the urban centers is given in Appendix 4.

c. Finance

14. The financial capacity of local government is at an early stage of development. The average revenue of the MCs in NWFP in 1998/99 was, excluding Peshawar, PRs15 million (\$0.3 million), with revenue ranging from PRs4 million to PRs52 million. The octroi tax, which was abolished in 1999, was the principal source of revenue, accounting for between 30 and 50 percent of MC revenue. Net revenue obtained from the octroi tax, a local tax, has been replaced with a grant from the federal Government using revenue from the general sales tax. While this change has been revenue neutral for individual local governments, it has resulted in substantially different rates of federal Government grants to local governments, ranging from PRs30 to PRs260 per capita in a sample of towns. Hence, the level of the federal grant has considerable influence on MC financial resources. While the federal Government has no plans to reform the grant, the current unequal distribution may be corrected, so relatively greater assistance is provided to poorer localities. The grant could also be provided on a matching basis to locally derived municipal income to encourage local resource mobilization. Such developments would have a significant impact on individual local government income.

15. Water rates typically account for about 10 percent of municipal revenue. Cost recovery for water supply is poor, with revenue being a little under half of O&M costs. Water tariffs are set by the NWFP government at a uniform rate for all towns, with the current monthly rate of PRs60 per household set in 1995. Municipal collection efficiency for water charges is about 70 percent. The NWFP Finance Department is currently proposing that the charge be increased to PRs85 per household per month, which will restore most of the decline in the real value of the current rate that has occurred due to inflation.

16. The immovable property tax is administered by the NWFP Excise and Taxation Department with the local town governments receiving 85 percent of the revenue collected. The tax base was changed in 1997 to a scaled flat rate related to property land area; this should provide a robust tax base. However, revenue from the tax falls far short of its potential. It provides an average of about 5 percent of municipal income, but varies considerably with the collection efficiency for individual towns ranging from almost zero to about 40 percent. Revenue from the combination of the grant from the federal Government, water sales, and the property tax account for over half of MC income, but is largely beyond their control. The MCs gain the remainder of their income from a range of sources; the most significant are a tax on transactions at cattle sales, charges for the use of bus terminals, and rent for municipal properties. Few local

governments impose charges for solid waste collection. Weak institutional capacity of the local governments and the low willingness by the general public to pay for services, which they have traditionally expected the Government to provide free of charge, has limited resource mobilization by local governments.

17. A little over half of MC expenditures are for staff. O&M expenditure is limited, and capital expenditure accounts for only 12 percent of total municipal expenditure. Total investment by the MCs and town committees in NWFP during 1996/97 to 1998/99 averaged PRs62 million per annum (in 1999 prices), equal to PRs22 per capita per year.

18. Local governments need to increase the mobilization of finances if they are to undertake basic O&M functions, and invest in infrastructure and human resource development. Considerable potential exists to increase local government revenue, especially from the immovable property tax and charges for water supply. However, increasing income from these two sources is largely dependent on the provincial government. The need for private sector participation in urban development is being increasingly recognized. Many towns in NWFP have started contracting out the collection of water tariffs and local taxes to private operators. The scope of private sector participation can be expanded, in part by withdrawing local government from commercial property activities.

19. The finance function of local governments has traditionally had a relatively low profile, and consequently demand has been low. The current system of accounting is simple, is undertaken almost exclusively using paper-based systems, and has the limited objective of securing the stewardship of cash. The taxation and financial management functions are administered through separate finance and taxation departments in each local government. Management information and budgeting are undertaken at a basic level only. LGERD obtains considerable information on local government finance, but makes little use of it. A previous study⁷ proposed that a more comprehensive accounting system based on double-entry accounting principles and improved budgeting and management information systems be adopted. The proposal, which has not yet been implemented, remains appropriate. The NWFP Finance Department is currently reexamining the proposal, with a view to implementing it.

B. Government Policies and Plans

1. Federal Programs and Strategies

20. Although progress was made in reducing poverty during the 1970s and 1980s, approximately 30 percent of the population still live in poverty and the incidence of poverty has been increasing over the past decade. The Pakistan Poverty Alleviation Fund, established in 1997 to finance income-generating projects, microenterprises, and infrastructure projects at the community level, mainly through nongovernment organizations (NGOs) and the private sector, has recently commenced its lending activities. In April 1999, the Government released a draft federal poverty strategy with the major objectives to (i) provide employment opportunities; (ii) promote sustainable economic growth; (iii) sustain growth using people friendly strategies that promote labor intensive employment and provide access to microfinance; (iv) expand and improve the quality of social services; (v) foster the development of community organizations to create social capital; (vi) focus on women as productive partners in development; (vii) mobilize government support organizations, especially NGOs; (viii) create safety nets for the poor; and (ix) support the evolution of an integrated approach that will create synergy through existing interventions. While strategy implementation is presently uncertain due to the indefinite postponement of the 1999 Pakistan Development Forum, where the policy was to be presented, the Government recently launched the National Poverty Alleviation Program with

⁷ TA 1248-PAK: *Urban Financial Management and Accounting*, for \$700,000, approved on 19 December 1989.

implementation commencing in March 2000. The program, which emphasizes stimulating employment opportunities and providing basic essential infrastructure and services to rural and low income urban areas, is now ready to commence implementing projects based on approved selection criteria for poverty-related projects. The type of projects that can be considered are identified under various subsectors, with those relating to low-income urban communities consisting of water supply systems, sewerage and solid waste management, drainage, provision of civic facilities, and maintenance of existing infrastructure. Each individual project will generally not exceed a cost of \$100,000 equivalent, and importance will be given to involving various communities and associated organizations in project selection, planning, and implementation. A first tranche of PRs600 million (approximately \$12 million) was released to NWFP, and the selection and approval of nominated projects is ongoing. The distribution of funds will be based on 40 percent for farm to market roads, 10 percent each for water supply schemes and sanitation projects, 10 percent for projects specifically involving women, and 30 percent for other eligible sectors. In each district, 25 percent of the projects will be selected in marginalized areas.

21. To address the present institutional shortcomings, particularly the delivery of basic services and facilities to the general public, the Government recently announced a program to devolve power and responsibility based on a bottom-up methodology, that is people-centered and customer service-oriented. The devolution program, contained in the Local Government Ordinance and promulgated in August 2001, is having significant impacts on the present system of local government, both administratively and financially. The local government design is based on five fundamentals: devolution of political power, decentralization of administrative authority, deconcentration of management functions, diffusion of the power-authority nexus, and distribution of resources to the district level. The present civil service is being transformed from rulers to service providers, while bringing about greater levels of accountability. Women are assured one-third representation on all union councils. The current fiscal transfer system from the federal to the provincial government is not subject to political approval, is not based on a transparent formula, is highly discretionary, and does not involve the district governments. Under the new Local Government Ordinance, more transparent, predictable, and equitable formulas are being established to determine fiscal transfers and grants from the province to the district level. At the same time, district and local governments will be encouraged to generate greater financial resources from their own constituencies, and to be less dependent on grants from federal and provincial governments. At this initial stage, the district administrations have been established within existing line departments, however, this administration system is envisaged to gradually move to a more corporate form of governance driven by a greater entrepreneurial approach. This will involve introducing a customer-service orientation, results-based management using achievement indicators, and staff performance evaluations based on monitoring by committees. In the long term, service contracts will be introduced that are renewable on the basis of performance and visible results in the improvement of the quality of life of the general public.

22. In response to the World Conservation Strategy launched in 1980, in 1992 the federal Government approved the National Conservation Strategy. Based on this strategy, in 1996 the NWFP cabinet approved the Sarhad Provincial Conservation Strategy. The strategy, developed using extensive public consultations, sectoral meetings, and thematic workshops, reflects provincial aspirations for sustainable development and a commitment package containing major policy statements, law reform initiatives, structural improvements, and new programs to achieve the strategy objectives. The specific objectives are to (i) address the fundamental social problems that are the underlying cause of environmental degradation; (ii) conserve, rehabilitate, and undertake sustainable development of natural resources; (iii) protect the living environment; (iv) develop high-quality environmental protection mechanisms including appropriate legislation, development planning mechanisms, environmental quality standards, and participatory and

regulatory institutional arrangements; (v) improve the institutional and financial capacity of the NWFP government to achieve sustainable development; (vi) protect and conserve the cultural heritage; (vii) increase community participation in environmental management; and (viii) raise public awareness and understanding of conservation and sustainable development. The strategy defines priority areas for action, including (i) governance and capacity development; (ii) poverty reduction and population; (iii) NGO, communication and education; (iv) urban environment and sustainable cities; (v) sustainable industrial development; (vi) natural resource management and biological diversity; and (vii) cultural heritage and sustainable tourism. While implementation of some of these initiatives has commenced, the full realization of the objectives must be viewed over the long term. The strategy provides a sound basis for sustainable development in NWFP.

23. The Eighth Five-year Plan (1993/94-1997/98) identified poor quality management as one of the major problems of the social sector, and recommended enhancing the absorptive capacity of the system through effective institutional reforms. The plan called for deliberate focus on the empowerment of communities and NGOs; and identified poverty reduction, promotion of good governance, and environmental protection as its major development objectives. With limited achievements under the plan, and in recognizing the need for institutional reform and improved governance at the provincial and local governments, the NWFP government, approved on 4 September 1999 the Action Plan for Restructuring and Strengthening Local Government. In general, the thrust of reforms is from the bottom-up. The emphasis on improving the capacity of local urban councils and municipalities is intended to percolate up through the system and influence the role and responsibilities of the provincial government. The plan identifies the need for changes in organizational culture. Recognizing the unacceptable state of urban services within towns, and with the objective of establishing an environment in which the delivery of public services can be improved and sustained, the NWFP government recently established an interdepartmental working group to assess the problems and to develop recommendations for institutional reforms. In line with the recent Government initiative to undertake greater devolution and decentralization of responsibilities to the local governments, part of the NWFP government's overall restructuring plan is to improve governance, including restructuring civil administration, consolidating existing administrative arrangements, identifying surplus staff of public service entities, enhancing tax collection, and increasing decentralization and devolution of administrative and financial authority and responsibility to the provincial, district, and local levels. Cost recovery will be a main policy and strategy item, and incremental user tariffs will need to be enforced to meet the entire expenditure for effective O&M of completed projects.

2. NWFP Urban Sector Framework and Investment Needs

a. Sector Framework

24. NWFP developed the Provincial Spatial Development Framework and Strategy for 2000/01-2019/20, with a provincial five-year plan (2000/01-2004/05). Details of the framework are given in Appendix 5. The objectives of the framework and strategy identify a number of policy issues and service standards that form the overall guiding parameters for future NWFP urban development initiatives. Under governance, the devolution of powers and responsibilities for planning, implementation, and management of urban development to local government units is the overall objective. This will be supported by strengthening local governments to enhance their capacity to carry out the devolved powers. With the absence of any real development planning tools, the development and implementation of urban structure plans will be undertaken to guide and control land use, and provide a basis for development and building control. To ensure enforcement of the plans, and to provide the necessary legal basis for their implementation, the structure plan will be codified within the legislative framework. The

application of appropriate, affordable (least cost), and balanced service standards will be the guiding principle when planning and delivering urban services. These standards will be applied in the process of investment planning, prioritizing, and budgeting for the development of infrastructure facilities. To ensure sustainability of urban infrastructure facilities, and to meet the priorities and aspirations of the urban communities, the focus will be on participatory planning techniques involving community-based organization (CBOs). The sector strategy will emphasize reducing existing environmental degradation in urban towns using a combination of physical infrastructure interventions, improved planning, community awareness programs, and enhanced O&M programs. Strengthening the capacity of local governments to raise local revenues, to cover at least the full cost of O&M of services, will be fundamental to any urban investment programs.

25. Urban centers in NWFP vary widely in the quality and coverage of basic urban infrastructure and services. The government has formulated targets for the provision of these basic needs, as a guide for planning and prioritizing investments in the urban centers. Given the wide disparities in infrastructure provision, a range of target standards has been defined, marked by low and high levels of service, with these targets to be reached by 2010. In addition, performance indicators were defined, as a basis for monitoring and evaluating project success.

26. In the project towns, from 25 to 83 percent of urban household currently have a piped water supply. Quality varies greatly with availability as low as 1-3 hours per day. Reducing the incidence of unaccounted for water and illegal connection is a focus of the strategy. The low target for 2010 is to achieve 50 percent coverage of the urban population, while the high target is 75 percent. Performance indicators include reaching the low target for 2010: installing water meters in 50 percent of households, improving the quality of service by adopting key performance indicators (water quality, pressure, hours of service), reducing unaccounted for water losses, and increased available revenue to be spent on O&M.

27. None of the proposed project towns have piped sewerage. Although many towns have expressed interest in full piped sewerage schemes with sewage treatment, such schemes are not considered realistic at the current levels of municipal income and available skills. Targets aim to improve the coverage of proper septic tanks (high: 75 percent, low: 40 percent), and improve septic tanks maintenance by introducing a septic tank maintenance service. Whether this service will be operated by the MC or contracted out to a private operator will depend on the MC's capacity. Performance indicators specify achieving the 2010 low target: the existence of a functioning septic tank cleaning service, and evidence of the installation of a septic tank for new buildings.

28. The central problem of the degraded living environment in all towns is related to the condition of the secondary and tertiary drainage systems, which invariably carry fecal waste. Targets for drainage improvement are difficult to express in quantitative terms. Rather, improvements are aimed at routine cleaning and rehabilitation of the existing systems, including the construction of road culverts. Performance indicators are formulated as an increase of real revenue spent on drainage system maintenance.

29. Coverage of domestic and commercial solid waste collection in the project towns ranges from 16 to 38 percent. These figures do not indicate the adequacy of the waste disposal methods. Targets are formulated as a percentage of population served (low: 40 percent, high: 60 percent) and as a fraction of the market waste collected (low: 80 percent, high: 90 percent). Performance indicators define that solid waste disposal should be operated by the private sector, with the use of formal disposal sites by 2005, and achievement of the low coverage targets by 2010.

30. Road maintenance in urban areas has been inadequate for many years. The MCs are responsible for most roads and associated roadside drains within their urban areas, with the exception of provincial and national roads. The existing road conditions are quantified in terms of the investment (PRs per capita) required to reach a predefined high and low standard. Values range from PRs400/capita to PRs2,000/capita to reach a low standard, and PRs1,300/capita to PRs5,000/capita to reach a high standard of road pavement. Targets are expressed as a percentage of roads in urban areas paved (low: 50 percent, high: 90 percent). Performance indicators specify achieving the 2010 low target: increased real revenue spent on road maintenance, as well as traffic management issues addressed in local plans.

b. Sector Investment Needs

31. Sector investment needs are based on actions needed to redress seriously deteriorated infrastructure and to expand infrastructure to service expected population growth. The urban population is expected to increase from 3.0 million in 1998 to 3.8 million in 2005, with average population growth of 3.4 percent per annum. An investment of about PRs4.8 billion (in 1999 prices) is needed in NWFP during 2000/01-2004/5 for remedial work on existing urban infrastructure. A further PRs13.8 billion is needed to provide the desired level of service to the increased urban population by 2004/05. Total needed investment until 2004/05 is therefore PRs18.6 billion, equal to an average of PRs3.1 billion per year (PRs835 per capita per year). If recent average annual investment in urban infrastructure by the local and provincial governments of about PRs0.4 billion continues, the financing gap will be PRs2.7 billion per year if future targets are to be achieved. This represents an ambitious capital investment program that will be difficult to implement in its entirety. Accordingly, desired investment projects will need to be prioritized to ensure that the maximum benefit is obtained from the available finance; and an acceptance that the desired targets will be difficult to achieve. Details of the sector investment needs are shown in Appendix 6.

C. External Assistance to the Sector

32. ADB has been involved in the urban sector in NWFP since 1989 with one loan (\$66.0 million) and three TAs (\$2.2 million). The loan,⁸ the SUDP, which was closed on 31 December 1999, included road construction, sewerage treatment plants, water supply, drainage, slum upgrading, and solid waste management in seven provincial towns. The TAs provided assistance with urban finance and management, and feasibility studies for priority investment components in selected towns, with policy recommendations for institutional restructuring and financial management. Another major external assistance to the urban sector in NWFP is the Community Infrastructure Project, for the provision of infrastructure upgrading for 55 rural and urban low-income communities. The project commenced in 1994, and was financed by the World Bank, the United Nation's Children Fund, and Swiss Agency for Development Cooperation. Details on external assistance to the urban sector in Pakistan is given in Appendix 7.

D. Lessons Learned

33. Portfolio performance has been constrained by a number of generic macro and micro issues, including (i) legal and administrative issues relating to processing procedures and requirements, (ii) coordination difficulties and procedural issues, (iii) technical and project management issues, and (iv) counterpart funding constraints and timely release. These issues result in implementation delays, with often negative financial and economic consequences. In addition, noncompliance with specific covenants, delay in consultant recruitment, minimal beneficiary participation, poor O&M of completed facilities, low financial and economic rates of

⁸ Loan 1004-PAK(SF), *Second Urban Development Project*, for \$66.0 million, approved on 19 December 1989.

return, and frequent changing of senior project management staff diminishes accountability and transparency, and undermines project sustainability.

34. An important lesson derived from the Karachi Urban Development Project⁹ is that urban upgrading is complex, and a piecemeal approach involving a few selected problems is not an optimal solution. Urban upgrading should be designed from a plan that integrates all aspects of urban infrastructure, and involves the participation of the ultimate beneficiaries. The institutional capacity to implement the project must be present, and the financial framework must be in place to ensure long-term sustainability of the upgrading. ADB's project performance audit report concluded that the Karachi Urban Development Project was unsuccessful, with the main identified weakness being in the design. Appendix 8 provides details of lessons learned from previous projects in the sector.

35. The design of the proposed Project takes this experience into account, in particular to (i) implement subprojects at the local level to develop greater ownership; (ii) use a competitive environment to select participating towns and subprojects; (iii) support subproject implementation and sustainability by obtaining financial contributions from participating towns, and enhancing the collection of taxes and fees from project beneficiaries; and (iv) develop a monitoring system to ensure effective implementation and accrual of benefits to the target groups.

E. ADB's Sector Strategy

36. ADB's operational strategy for Pakistan supports human resource development and social infrastructure requirements, as well as programs to respond to the policy environment, including increased priority for macroeconomic management and support for economic stabilization and restructuring. With ADB's emphasis on poverty reduction, and the challenge to deliver basic services to the people, resources must be effectively used, especially to reduce poverty in an environment of effective economic management, good governance, and strong policy commitment. The main focus of ADB assistance to the urban sector will be on environmental aspects and the needs of the poor, and will broadly cover (i) institutional restructuring emphasizing eliminating overlapping functional responsibilities, professionalizing urban management, developing staffing policies, and devolving service delivery; (ii) private sector involvement in the delivery of selected urban services; (iii) budgeting and finance, and increased cost recovery and municipal revenue; and (iv) increased community participation. Capacity building efforts will be pursued for institutional strengthening of provincial and municipal urban management and operations, including planning and implementation capabilities, financial management, and environment management. Identified strategic considerations for the urban sector include (i) establishing service levels, affordability, and beneficiaries' willingness to pay; (ii) implementing cost recovery; (iii) minimizing environmental impacts; (iv) targeting low-income groups; (v) integrating health service provision; and (vi) supporting community participation.

37. The demand-oriented planning approach is considered best practice, and requires involving beneficiaries in design, technology choice, implementation, and operations; and allowing flexibility in project design and service levels. This project participatory design methodology is central to ADB's sector development strategy. While in urban areas sector interventions are tied to measures to conserve environmental resources, public sector management capacity and accountability remain major constraints to satisfactory social sector development. Improving existing service delivery mechanisms is essential to achieving sustainability and will be used to encourage private sector participation and NGO involvement.

⁹ Loan 793-PAK(SF): *Karachi Urban Development*, for \$55.20 million, approved on 14 October 1986.

Public sector management requires decentralizing decision-making authority, policy reforms for local revenue generation capacity, and cost recovery for urban services.

F. Policy Dialogue

38. Since commencement of its assistance to the urban sector in the mid-1980s, ADB has continuously discussed issues and policies in the sector with the Government, particularly (i) improving governance; (ii) enhancing service delivery; (iii) ensuring financial and administrative autonomy for urban service providers; (iv) implementing cost recovery and sound financial management; (v) institutionalizing community participation; and (vi) providing greater equity in the delivery of municipal services, particularly for the low income and disadvantaged groups within the community. ADB has noted with concern the lack of progress made in the NWFP urban sector to strengthen the planning, management, and financing capacity of local governments. The Urban Sector Policy Action Plan outlines a clear set of objectives and tasks for NWFP over the next five years to improve governance, financial strengthening, and resource mobilization, O&M, rehabilitation capability, and environmental protection. These objectives fully complement the Government's devolution initiatives.

39. In view of the current limited capacity of local government for forward planning and raising financial resources, ADB's investment in the sector will be (i) strictly limited to high-priority basic needs of the urban poor, (ii) linked with capacity building programs for urban financial management and urban development planning, and (iii) simultaneous with programs aimed to strengthen the municipal capacity for community participation. ADB recognizes the overriding importance of continuous training and education, taking into account the basic levels of skills and awareness in small urban communities in NWFP. The federal Government has developed new initiatives to devolve power and responsibility to local governments, and reduce poverty. Given this background, the urban policy for NWFP is formulated to support the Government's devolution and poverty reduction initiatives.

1. Decentralization and Devolution

40. The Government's policy of decentralization and devolution is critical to developing a greater local responsibility. Unless greater accountability at the local level can be developed and management improved, efficient and cost-effective services to the community cannot be achieved. The mobilization of local resources and improved management of existing infrastructure and services are paramount to achieving these objectives.

41. The federal Government has agreed that the Project will support these objectives by (i) strengthening the managerial, financial, and technical capacity of the MCs by giving them more responsibility, and upgrading the capability and capacity of their staff; (ii) providing adequate staff, equipment, and procedures to enable the MCs to increase resource mobilization, successfully implement and sustain subprojects, and improve the management and delivery of existing urban infrastructure and services; and (iii) providing a training program for the MCs and provincial staff to develop their technical proficiency. The Government has made a commitment to aim at greater continuity in the appointment of key professional and administrative staff in local councils.

2. The Urban Poor

42. The Government is committed to providing support for low-income groups, and responding to their needs in prioritizing development programs and evaluating the performance of urban services that will affect them. ADB has encouraged the urban poor to participate in these processes to ensure the effective implementation of projects that meet user needs, and to enhance equity and sustainability in urban service provision. ADB has also encouraged the

Government to ensure that the benefits of activities intended to support the poor are delivered to target beneficiaries. The Project, through its basic human needs approach, with emphasis on providing improved services to lower income groups within the urban community, is designed to support these objectives.

3. Urban Planning and Development Control

43. ADB recognizes that the absence of a clear legal and institutional framework for urban land-use planning and development control is a crucial deficiency when improving urban management. The concept of structure plans as a guide for medium-term planning is (i) not present in current legislation, and (ii) little known as a professional planning tool for urban sector staff. Revision of the legislative and institutional framework to allow for an improved basis of planning will require broad discussion and agreement at federal and provincial levels, and can therefore not be achieved in the short term. ADB will therefore continue to support government in its aims to make practical improvement at the local level, by introducing the concepts of urban planning to urban government staff as part of its capacity building program. Simultaneously, ADB will continue its involvement in the longer-term review of the legislative and institutional framework of NWFP's urban sector. Under the Project, each participating town will be required to have an up-to-date base map, with the outline of an urban structure plan as a guide for future development. The Project will provide support for the development of structure plans that will ultimately form the basis for improved municipal management and enhanced implementation of the immovable property tax system.

4. Communication between Local Government and Communities

44. Both ADB and the Government recognize the current reluctance of the urban population to contribute to urban services through taxes or charges, largely because they lack confidence in local government to deliver any form of services to the benefit of the population. The drive to raising more local revenues by collecting taxes and charges can only succeed if government is seen to improve the quality of its services. This will require improved communication between civic society and local government, as well as an improved understanding by local government staff on their responsibility to provide service to the urban population. The Project will emphasize developing forms and mechanisms for community participation that are appropriate to the sociocultural and political environment of urban communities. The development of sustainable partnerships between community groups and local government will be a key objective of the Project to develop effective and lasting channels of communication.

5. Municipal Capacity for Community Participation

45. ADB is committed to supporting the Government's efforts to increase participatory planning in urban management and development. To achieve this in government structures with little direct exposure to such techniques, ADB recognizes the need to understand the problems that local government will experience in planning and implementing participatory processes, the options for resolution, and the nature and extent of capacity building required. In program preparation, three primary areas will be identified where a better understanding as well as immediate action is required: (i) the nature of participation and partnerships with poor communities, (ii) the mechanisms for establishing community participation, and (iii) the institutional change necessary to integrate participatory processes with current operations.

IV. THE PROPOSED PROJECT

A. Rationale

46. Urban areas in NWFP are experiencing rapid growth, and demand for improved urban service is increasing. Current deficiencies in basic infrastructure are inhibiting economic growth, and severely constraining the potential for urban areas to play a more significant role in NWFP'S economic growth. To meet the growing pressures and demands, urban development has usually occurred with little or no environmental controls and with forms of governance that cannot begin to meet the responsibilities. High urban growth combined with slow urban sector development has resulted in uncontrolled urban sprawl; deteriorating urban environments; and deficiencies in all forms of urban services, including water supply, sewerage systems, drainage, solid waste management, roads, and community facilities. Lack of urban planning, land-use control, and construction regulations in almost all urban centers in NWFP has resulted in unplanned, ad hoc town developments, with the emergence of many slum areas.

47. Although on average 39 percent of NWFP'S urban population have access to piped water supply, the quality of drinking water is often low due to the aging distribution system, lack of local treatment facilities, and contaminated water sources in some urban centers. System losses are high and supply irregular, often providing for less than six hours per day. Sewerage systems and drainage networks are totally insufficient in most towns, particularly in the low-income settlements, where localized flooding causes unhygienic conditions and seriously impacts on the living conditions of the residents. In most urban towns, clinical, industrial, and commercial sewage is discharged into open drains and canals without treatment. Wastewater from leaking sewers, unlined drainage canals, septic tanks, and open ponds percolates into the soil and contaminates the shallow water aquifers from which most people draw their drinking water. Solid waste management in the majority of urban towns is at best rudimentary. Approximately 50 percent of the total generated solid waste is collected and the remainder is left uncollected and disposed of in waterways and open fields. This results in blocked drainage systems, flooding, and environmental pollution.

48. Of the 46 classified urban centers in NWFP, 7 towns participated in the SUDP leaving a remainder of 39 urban centers to be considered for the proposed Project. Towns will be selected for inclusion in the Project based on a series of assessments of key factors that include (i) administrative status (headquarters of either a division, district, or tehsil), (ii) availability of a base map of the town, (iii) population size greater than 20,000 persons, (iv) population growth rate, (v) level and availability of social infrastructure, (vi) capability and interest of the local government, and (vii) economic potential. Of the 24 urban centers meeting the criteria for administrative status and population size, seven towns that meet all the criteria were selected as first-phase towns under the Project.

49. The Project is formulated as a sector loan based on the NWFP government's overall long-term sector requirements for 2001-2020. It will support the Government's poverty reduction initiatives, as well as the forthcoming devolution of power and responsibility to the local governments for the provision and financing of urban infrastructure and municipal services. The Project incorporates several strategic features and incentives for participation in the Project including (i) promotion of policy reform in the sector, particularly financial management and resource generation at the local government level; (ii) priority to investments that meet the basic needs of urban communities; (iii) local community participation and ownership; and (iv) equity participation by local governments in the investment packages.

50. The Project meets the criteria for adopting a sector lending modality. A workable urban sector framework and strategy exists, and LGERD has the legal mandate for administration of

the local governments, for planning, finance, and infrastructure development. In addition, LGERD has the lead responsibility for implementing the Government's devolution and poverty reduction programs. The Project will also support ADB's urban sector strategic objectives, especially for use of participatory approaches, institutional development, devolution of service delivery, targeting of low-income communities, financial equity, and cost recovery. The Government and ADB have agreed on the criteria for town participation, selection of subprojects, and appraisal standards.

B. Objectives and Scope

51. The overall objectives of the Project are to support the (i) devolution of responsibility and authority to local governments by expediting the policy reform process in the sector; (ii) decentralization of economic growth to reduce provincewide disparities; and (iii) reduction of urban infrastructure deficiencies in urban areas. The Project's specific objectives are to (i) demonstrate effective interventions in urban services management that can be replicated, (ii) stimulate a progressive shift of responsibilities to urban local governments for financing and management of urban services, and (iii) improve management and resource mobilization capacities of urban local governments.

52. The Project covers up to 24 urban centers in NWFP, classified as MCs (excluding 7 urban centers, including Peshawar, included under the SUDP), with a total population of approximately 1.0 million, or around 32 percent of the overall provincial urban population. The Project gives priority to seven of these centers, which are generally representative of the urban sector, including Charsadda, Hangu, Haripur, Mansehra, Takht Bhai, Timargara, and Swabi, with a total project population of around 400,000. Each of the seven centers has an outlined structure plan, five-year investment plan, urban profile, and detailed feasibility studies of proposed subprojects.

53. The Project has two main components: (i) urban development, including infrastructure improvements and community development and participation; and (ii) institutional development, including project implementation support, municipal finance capacity building, and incremental administrative support. A description of these components follows and summary of the prepared subprojects is given in Appendix 9.

1. Urban Development Component

54. The urban development component comprises infrastructure improvements and community development and participation, and includes town-specific investments in one or more infrastructure improvement subprojects, and formation of CBOs. The component will complement the Government's initiatives under its Poverty Alleviation Program.

a. Infrastructure Improvements

55. **Water Supply.** Subprojects will be designed to improve the service quality of existing schemes, and increase revenues through a combination of leak-detection programs and the conversion of illegal connections to registered accounts. Where necessary, distribution systems will be extended to, or improved for, poorly served areas. Priority will be given to servicing low-income areas. Consideration will be given to installing water meters in towns that have achieved a secure 24-hour supply system, and that can demonstrate the technical and management discipline required to run a meter-based billing system.

56. **Sewerage and Sanitation.** Subprojects will aim to improve the disposal of human waste by increasing the use of small sewerage schemes with local treatment, encouraging the installation of adequately designed individual and communal septic tanks, and improving the

maintenance of septic tanks by introducing septic tank maintenance services. Whether this service will be operated by the MC or contracted out to a private operator will depend on the MC's capacity, and realistic projections of the potential revenue resulting from service charges.

57. **Drainage.** Subprojects will focus on routine cleaning and rehabilitation of existing systems, with particular emphasis on the interconnection of isolated stretches of drainage channels into a fully integrated drainage network. Priority areas will be high-density, low-income areas, where project intervention will result in a marked improvement of living conditions. Investments in new works will focus on establishing drainage networks including suitable outfalls. Drainage subprojects will all include the establishment of maintenance procedures and systems, and where necessary, supported by the provision of basic drainage cleaning equipment.

58. **Solid Waste Management.** Subprojects will aim at minimal investment for collection systems, thereby requiring community support through waste minimization and the concentration of waste to neighborhood collection points. Emphasis will be placed on increasing the cash contribution from commercial establishments. Where waste collection equipment is to be provided under the subproject, it will be based on practicality and affordability, and appropriate to the particular urban environment. Waste disposal sites and new landfill developments will be supported contingent upon the identification of suitable disposal sites that meet established environmental guidelines and controls.

59. **Roads and Local Access.** Subprojects in the road sector will rehabilitate and improve the main urban road network by resurfacing and widening within the existing right-of-way. Improved access to the town center and local neighborhoods will increase economic opportunities by attracting investment. Road projects include the improvement of associated roadside drains. Part of the subproject will involve traffic management measures to improve circulation in congested town-center areas, through junction improvement and introducing restrictions on parking and roadside vending. Other subprojects will include the extension of the road network, and opening up new areas for controlled development.

b. Community Development and Participation

60. This subcomponent will aim to develop organizational and human capacity within local government for participatory processes targeted at poverty reduction and basic needs programs. During project preparation, a socioeconomic survey was undertaken in the seven first-phase towns, along with public hearings, group interviews, and a selected household survey. In addition, consultations with NGOs and CBOs were initiated during the various town meetings. Where possible, households headed by women were interviewed to develop a better understanding of their problems and perceived priorities. Urban sector policies in the past were fragmented and resulted in a serious erosion of public trust in state mechanisms and their ability to provide sustainable public facilities and services to urban communities. As a consequence, the increase in self-help initiatives and in new partnerships between communities, NGOs, and the private sector is significant. Under the Project, CBOs will be established, where they do not exist within the participating town, and mechanisms established to develop greater partnerships between the communities and local governments. For existing CBOs, these relationships will be strengthened, with greater focus on this partnership role, and the development of better municipal management.

2. Institutional Development Component

61. The institutional development component consists of project implementation support, municipal finance capacity building, and incremental administration support, all linked to support the Government's devolution program, while building the capacity of urban local governments.

a. Project Implementation Support

62. Involvement in the Project will encourage the MCs to take a more active role in planning, preparing, designing, and managing the implementation of development initiatives within their area, to the benefit of their constituency, largely consisting of the urban poor. Commitment to such involvement is required for participation in the Project. The MCs will be helped to establish, from within their own ranks, a project implementation team (PIT) dedicated to project preparation and implementation. The management of the entire project cycle is the primary responsibility of the MC, with the Project's project coordination unit (PCU) and its TA team taking a guiding and monitoring role.

b. Municipal Finance and Capacity Building

63. In recognition of the critical importance of improved financial performance and increased revenue collection by the MCs, a specific component of the Project's institutional development is dedicated to improving municipal financial management, by introducing improved accounting procedures and management information systems. With greater devolution of power to the local government levels, especially for the management of urban services, along with greater fiscal autonomy, the development of improved financial management systems and enhanced resource generation is critical to the long-term sustainability of the urban centers. With the assistance of the consultants, the MCs will develop and implement a computerized accounting system; improved financial management and information systems, including budgeting, resource mobilization, and enhanced O&M of existing assets; and improved billing and collection systems.

c. Incremental Administration Support

64. Incremental administrative support for project implementation is required for the provincial and local governments. A PCU, consisting of LGERD staff, will be responsible for provincial coordination, planning, and management of project activities. A team of 12 professional staff, representing various disciplines, and administrative support staff, will be required. At the local level, a PIT will be established in each participating town to oversee subproject planning, design, and implementation; and maintain close linkages with associated NGOs and CBOs. One of the major objectives of this subcomponent is to develop greater ownership at the town level.

C. Cost Estimates

65. The Project is estimated to cost \$30.0 million equivalent, with foreign exchange costs of about \$8.7 million, or about 29 percent of the total project cost, including \$0.5 million for interest during construction. Local currency costs are \$21.3 million equivalent, or about 71 percent of the total project cost. The cost of the infrastructure component includes civil works, equipment and materials, survey, and detailed design and supervision. Table 1 provides summary of the project costs.

Table 1: Cost Estimates
(\$ million)

Item	Foreign Exchange	Local Currency ^a	Total Cost
A. Urban Development Component			
Infrastructure Improvements	6.8	16.8	23.6
Community Development and Participation	0.0	0.7	0.7
Subtotal (A)	6.8	17.5	24.3
B. Institutional Development Component			
Implementation Support	0.8	0.8	1.6
Municipal Finance Capacity Building	0.7	0.5	1.2
Incremental Administration	0.0	2.5	2.5
Subtotal (B)	1.5	3.8	5.3
Interest During Construction	0.4	0.0	0.4
Total	8.7	21.3	30.0
Percent	29%	71%	100%

^a Taxes and duties are estimated to be about \$3 million.

D. Financing Plan

66. The proposed ADB loan is for \$20.8 million equivalent from the Special Funds resources, which will represent 69 percent of the total project cost. The loan will cover 98 percent of the foreign exchange cost component of the Project and 58 percent of the local currency cost, excluding taxes. The Borrower will be the Islamic Republic of Pakistan. The Borrower will pass on loan funds to NWFP on the same terms and conditions as those between ADB and the Borrower. The Borrower will assume the foreign exchange risk on the loan. NWFP, together with the participating MCs, will cover the remaining 31 percent of the project cost, approximately \$9.2 million equivalent, which includes (i) \$7.4 million equivalent from NWFP, including \$0.25 million in foreign currency cost for funding the international municipal finance management advisor position of 13 person-months under the Institutional Development Component; and (ii) \$1.8 million equivalent from the MCs for incremental administration. ADB's financing of local currency expenditure is justified by the nature of the Project, which will improve the living and health conditions of the people in the project areas by upgrading existing unsanitary conditions, improving water supply services, and preventing damage to property and disruption of lives caused by localized flooding. Communities will contribute to the cost of implementing and sustaining sanitation and drainage subprojects where practicable. A summary of the financing arrangements is shown in Table 2.

67. The MCs will be required to finance the incremental administration cost associated with their involvement in the Project, and a minimum of 20 percent of the cost of town-specific subproject capital works costs, increasing to a maximum of 50 percent based on the MC's current and projected financial capacity at the time of subproject approval, through subloans using project funds. This loan proportion takes account of the MCs' financial capacity, including ability to impose user fees for full cost-recovery purposes. Tripartite subsidiary project agreements, including grant and subloan components, will be entered into between the NWFP Department of Finance, LGERD, and the participating MCs. Subloans to the MCs will be at an interest rate of 7 percent per annum, with a grace period of 3 years and repayment of principal over a subsequent 12-year period. The subsidiary project agreements will include standard terms and conditions for implementation of the subproject, and will be supported by a loan agreement between the NWFP Department of Finance and the Ministry of Finance. As subloans

are repaid, the NWFP Department of Finance has the opportunity to relend funds to other project MCs and other local governments for investment in urban infrastructure, thus enhancing the sustainability of future urban sector investment by local governments. Funds will be repaid to the Ministry of Finance, according to its debt service obligations on the ADB loan. Details of the proposed financing arrangements are shown in Appendix 10.

Table 2: Financing Plan^a
(\$ million)

Source	Foreign Exchange	Local Currency	Total Cost	Percent
ADB	8.5	12.3	20.8	69
NWFP Government	0.2	7.2	7.4	25
Municipal Committees	0.0	1.8 ^b	1.8	6
Total	8.7	21.3	30.0	100

ADB = Asian Development Bank, NWFP = North-West Frontier Province.

^a Excludes beneficiary contributions to sanitation subprojects.

^b Based on cost of incremental administration by MCs.

E. Executing Agency

68. The Executing Agency for the Project will be the NWFP government through LGERD.

F. Implementation Arrangements

1. Implementing Agencies

69. A project steering committee will be established prior to loan effectiveness to oversee the Project, and to be chaired by the Secretary LGERD, with committee members consisting of representatives from DOF, PDD, WSD, and departments handling the functions of PPHD, PHED and environmental concerns. The steering committee will meet at least twice a year and as often as required.

70. The PCU, established in LGERD before loan negotiations, will (i) prepare the overall project implementation plan and the consolidated annual work plan, (ii) coordinate and appraise subproject proposals, (iii) provide technical support and supervision functions for subproject implementation, (iv) plan and coordinate activities to improve local government financial management, (v) plan and guide community participation, (vi) advise on terms of reference and consultant selection for design and supervision of subprojects, (vii) facilitate project coordination, (viii) prepare consolidated progress reports and documentation, (ix) organize project performance monitoring system (PPMS) activities, and (x) prepare the project completion report. The PCU's large agenda of activities range from the continual monitoring of MC participation criteria to providing technical support and supervisory functions for subproject implementation. The PCU will be headed by a Project Director from LGERD and have 12 professional staff, supported by international and domestic consultants.

71. At the local government level, PITs will be established within each participating MC to manage subproject implementation. Procurement of goods and services for all subprojects will be initiated by the PITs and will be ratified by a local bid evaluation committee, including representation from the MC, PCU, and district councils. Each PIT will comprise four professional staff, identified from the MC's permanent professional cadre, and managed by a senior engineer. Details of the project organization are given in Appendix 11.

2. Participation in the Project

a. Criteria

72. Urban towns to be included in the Project will need to show willingness to provide technical staff to manage and implement the subprojects, and adequate financial capacity to service debt requirements. Subprojects¹⁰ will be identified and prepared through a subproject planning and appraisal process under which user demands, and financial, economic, and affordability considerations are fully integrated with technical, environmental, social, and institutional factors. Least-cost technical solutions will be a focus of the subprojects. A total of 11 core subprojects were prepared during the TA; these subprojects are representative of the high priority urban infrastructure improvements in accordance with the needs of the first-phase participating urban towns, and in the context of the town's development plans. Based on the current financial and management capacity of the first-phase towns, the proposed core subprojects include water supply, sewerage and drainage, solid waste management, and road improvements. Their financial internal rates of return range from 6 to 17 percent.

73. Entry participation of MCs in the Project will be conditional on (i) setting up a PIT from the existing staff cadre, consisting of at least a senior qualified municipal engineer, bookkeeper, clerk, and senior officer to be assigned as a community liaison officer; (ii) undertaking to implement an updated improved accounting system and management information systems to be provided under the Project; (iii) committing to increase revenues to implement proposed subprojects; (iv) agreeing to finance a minimum of 20 percent of subproject capital works cost, and up to a maximum of 50 percent based on the current and projected financial capacity; (v) having an up-to-date base map, with the outline of an urban structure plan as a guide for future development; and (vi) providing evidence of preparedness to implement an improved municipal finance and accounting procedures.

b. Subproject Selection and Preparation

74. Subprojects will be located in participating project towns throughout NWFP, and will be small to moderate in value (most will be between \$100,000 and \$1 million equivalent). Priority subproject investments will be identified by the MCs; feasibility studies will be prepared by the PIT, appraised by the PCU, and approved by ADB. Management action and financial plans prepared by the MCs upon acceptance into the Project will be updated as required to ensure that the MCs implement actions required to continue development of long-term technical and financial capacity. This process will ensure that the proposed investments are focused, respond to local basic needs and demand for services, designed to appropriate standards, suitably justified, and sustainable. Prior to approval of any subproject, the MC will have undertaken the following actions to improve its financial capacity: (i) register all water connections; (ii) ensure that the immovable property tax register has been updated; (iii) identify potential municipal income at least for water fees and immovable property tax, and current and potential collection efficiencies; (iv) develop a time-bound action plan, in coordination with the provincial urban sector policy action plan, to increase revenue at least from water fees and immovable property tax; and (v) agree to implement a program of user fees for solid waste collection and cleaning of septic tanks.

75. Requests for subprojects with outline project description, and rationale will originate from the MCs. Successful subprojects will provide basic urban services and needs, be directly aimed at poverty reduction and improving economic opportunities, and have a low investment with emphasis on improved processes for rehabilitating and maintaining existing municipal assets.

¹⁰ A subproject is defined as an urban infrastructure investment package in a single subsector.

Aggregate investment for subprojects per town will not exceed the equivalent of \$1 million. Following confirmation that the proposed subproject(s) meet the agreed eligibility criteria for funding under the Project, the MC through its PIT will proceed with subproject preparation, with technical guidance from the project staff at the PCU when required. Subproject appraisal reports will include (i) the rationale, scope, target beneficiaries, design standards, cost, and implementation and procurement arrangements; (ii) environmental clearances, and social, economic, and financial justification; (iii) evidence of technical, managerial, and financial performance of the MC to demonstrate that it will be able to cover O&M costs and debt service associated with the proposed subproject; and (iv) identification of actions to update the MC's management and financial action plan to take into account the proposed subproject. Feasibility studies will be documented in standardized subproject appraisal reports.

76. Following approval by ADB, the MC will sign a subsidiary project agreement with the Department of Finance, and with LGERD as a party to the agreement, regarding the loan and grant component of the subproject. This agreement will describe any conditions and covenants that must be satisfied by the MC before or during subproject implementation. Prior to signing, the first subsidiary project agreement will be submitted to ADB for approval.

c. Community Participation

77. Particular emphasis will be given to developing forms and mechanisms for community participation that are appropriate to the sociocultural and political environment of urban communities in small towns in NWFP. Lessons can be learned from the successful establishment of CBOs as a means to plan and deliver small-scale infrastructure improvements within the Community Infrastructure Program in NWFP. While these were predominantly in rural areas, important lessons can nevertheless be drawn. Participatory techniques need to be designed to improve communication between community groups and government, and to make government more responsive to the priority needs of its constituency.

78. The community participation component of the program will be planned and designed by the community development adviser as part of the institutional development team to the PCU. For project towns, mechanisms need to be established to organize and mobilize communities to participate in improving delivery of urban services in general, and in the project activities in particular. The form, nature, and mechanism of this participation will vary depending on the type of subproject, and the interests, willingness, and skills of the community. The integration of the participatory processes with current operations will be a focus of the community participation component.

79. The Project will include one or more NWFP-based NGOs to establish sustainable government-community partnerships in the development of effective and lasting channels of communication. The NGO activities will be coordinated by the community development adviser in the PCU. The objectives of the NGO involvement will be to (i) jointly determine the appropriate nature and extent of community participation; (ii) assist with formulating suitable mechanisms for government-community interaction; and (iii) develop organizational and human capacity within local government for participatory processes aimed at poverty reduction and basic needs activities.

3. Consulting Services

80. To support Project implementation, 396 person-months of consulting services (36 person-months international and 360 person-months domestic) will be required, covering (i) project management support to the PCU and PITs, including subproject preparation and appraisal, and capacity building for subproject implementation by local government agencies (214 person-months); and (ii) capacity building for municipal financial management to the MCs,

to improve accounting systems and increase local revenues (182 person-months). Consultants will support staff within LGERD and the MCs. The consultants will be engaged through a firm in accordance with ADB's *Guidelines on the Use of Consultants* and other arrangements satisfactory to ADB for the engagement of domestic consultants. In addition, one or more NWFP-based NGOs, to be recruited by the government, in consultation with ADB, and in accordance with guidelines established in PDD for NGO recruitment, will be involved in the process of establishing sustainable government-community partnerships, for the development of effective and lasting channels of communication. Outline terms of reference for consultants are given in Appendix 12.

4. Procurement

81. Procurement will generally be carried out by the MCs under the guidance of the PCU. All procurement will follow ADB's *Guidelines for Procurement*. Since most of the project sites will be small and scattered, the Project is not likely to attract international civil works contractors. All civil works subprojects are expected to be less than \$1.0 million and will therefore be undertaken through local competitive bidding in accordance with procedures acceptable to ADB. Each subproject should be procured as a single contract. Where the contract value exceeds \$1.0 million, the contract will be procured through international competitive bidding procedures. Equipment items that are locally available and cost more than \$50,000 equivalent and less than \$100,000 equivalent may be procured through local competitive bidding, while items costing less than \$50,000 may be procured through direct purchase in accordance with procedures acceptable to ADB. International shopping will be followed for materials and equipment packages estimated to cost more than \$100,000 but less than \$500,000 equivalent, while materials and equipment packages costing in excess of \$500,000 equivalent will be procured through international competitive bidding procedures. All procurement will be channeled through the PCU for concurrence prior to submission to ADB for approval.

5. Disbursement

82. To ensure the timely release of loan proceeds and to expedite project implementation, and subject to ADB's assessment of the accounting systems and internal control of LGERD, an imprest account will be established in LGERD promptly after loan effectiveness. The establishment and operation of the imprest account will be in accordance with ADB's *Loan Disbursement Handbook*. The initial deposit to the imprest account will be based on estimated expenditures for the first four months of project implementation, but will not exceed the equivalent of \$200,000. ADB's statement of expenditure procedure may be used for reimbursement of eligible expenditures and to liquidate advances to the imprest account. The statement of expenditures procedure will be applicable to contracts amounting to \$50,000 or less.

6. Operation and Maintenance

83. Responsibility for O&M of the project facilities will rest with the MCs. Communities will also play an important role in O&M, particularly for solid waste management and drainage maintenance, where community involvement and active participation is critical. Routine maintenance in urban centers in NWFP has deteriorated over recent years, as a result of inadequate funding, ill-defined responsibilities, and lack of a service-oriented perception/attitude in local government. The emphasis placed in the institutional development component of the Project to improve financial management and increase MCs' resource generation is largely aimed at reversing this trend. Project guidance and monitoring by the PCU will focus on evidence of tangible improvement in O&M. Increasing community awareness of the MCs' constitutional responsibility for O&M will apply pressure to council staff to improve performance,

while simultaneously identifying a role for community groups in neighborhood maintenance. Subproject agreements will emphasize adequate O&M of subprojects as a condition for financial support.

7. Land Acquisition and Resettlement

84. By their nature, only solid waste disposal, drainage, and road improvement subprojects can be expected to require any land acquisition, and even this will be minimal. During project preparation, no land acquisition or resettlement was identified for core subprojects. The approval of subproject appraisal reports will be conditional on the inclusion of a detailed timetable for land acquisition that is acceptable to ADB. Resettlement of people is unlikely. If involuntary resettlement is unavoidable, a resettlement plan will be prepared by the MC, with the assistance of the project consultants and in consultation with the community. The resettlement plan, which will be in accordance with ADB's Policy on Involuntary Resettlement and the Handbook on Resettlement, 1998, will be submitted to ADB for its review and approval as part of the subproject appraisal report.

8. Public-Private and Community Partnerships

85. Some of the subprojects proposed appear suitable for private sector involvement with O&M. In particular, the solid waste management and the septic tank desludging service promoted as part of the Project are primary targets for private sector operation. However, current conditions in MCs are not immediately conducive to effective public-private partnerships. The present record on cost recovery of basic services by collecting fees and charges is such that local entrepreneurs are unlikely to be interested in assuming service contracts. In addition, the MCs have had little or no experience in formulating or effectively managing private sector service contracts.

86. The potential for community partnerships in the delivery of urban services, the form of participation developed, and the role of each partner will be influenced by the complexity of work to be undertaken and the degree to which the community feels ownership of the work being carried out. The array of service types (water, sanitation, solid waste, etc.), the scale of these services (primary, secondary, or tertiary), and stage of their implementation (planning, construction, or maintenance) create a range of opportunities for participation. Therefore, service delivery must be disaggregated, to consider the potential roles of partners at the different levels and to integrate these into a practical implementation proposal.

9. Implementation Schedule

87. The Project will be implemented over six years, beginning in early 2002, with completion by 31 December 2007. The Project is expected to be undertaken in three phases, with three batches of provincial towns. Phase 1 will involve seven towns, with subprojects already appraised, and ready for detailed design and implementation. Subprojects for phases 2 and 3 will include groups of about five towns that come on stream in years 2 and 3, at approximately 18-month intervals. The six-year implementation period is considered appropriate, given the large number of subprojects, the geographic spread of the Project, and the institutional capacity of the local governments. The project implementation schedule is in Appendix 13.

10. Monitoring and Reporting

a. Midterm Review

88. A midterm review will be carried out within three years of loan effectiveness. The review will include a comprehensive evaluation of the project implementation arrangements, with progress checked against the designed targets, consultations with community groups, and a review of the institutional and policy development aspects.

b. Project Performance Monitoring System

89. The Government will ensure that a comprehensive performance monitoring program acceptable to ADB is implemented to monitor and evaluate the technical performance and social and economic benefits of the Project, especially to the poor and women. The performance monitoring indicators and procedures will be tested with respect to data availability and other constraints, revised if necessary, and institutionalized as part of the Project's management information system. Participating towns will be responsible for undertaking periodic monitoring and assessment of the performance monitoring activities for subprojects. To measure the project impacts on the beneficiaries, particularly marginalized groups within participating towns, accurate baseline information must be established at the commencement of subproject implementation, with this information being the basis for determining the resulting impacts. Monitorable indicators will consist of (i) institutional development indicators covering revenue generation and financial management, along with O&M; (ii) subproject implementation indicators for the various categories and types of urban infrastructure, including levels of coverage and service delivery; and (iii) sectoral impact indicators, covering economic growth, public health, and community participation aspects.

c. Reports, Accounts, and Audit

90. The Government will provide ADB with quarterly progress reports on project implementation. The progress reports, to be prepared by the PITs and consolidated by the PCU, will provide a narrative description of project progress during the period, any modifications to the project schedule, problems and difficulties experienced, and a description of the work to be carried out in the next period. The progress reports will provide summary financial accounts for the Project consisting of project expenditures during the quarter, year-to-date expenditures, and total expenditures to date. The PCU will address the institutional and policy development aspects of the Project, and maintain separate accounts for the Project. Detailed annual project accounts and statements of the imprest account will be submitted to ADB in audited form within 9 months of the close of the fiscal year. The auditor appointed to audit the accounts will be acceptable to ADB. LGERD will submit to ADB, within three months of physical completion of the Project, a project completion report that will cover the details of project implementation, costs, BME activities and results at that time, compliance with loan covenants, and other information that may be requested by ADB.

d. Management and Financial Action Plans

91. The need to define a base from which improved financial and technical management capabilities of the MCs can be developed is essential for long-term sustainability of urban infrastructure provision. The means of subsequent management improvement will only flow from future actions of (i) the MCs; (ii) the NWFP Government through its influence on water tariffs and collection of the immovable property tax; and (iii) support and changes in the environment in which the MCs operate, and promoted as a result of the devolution initiatives of the federal Government. Financial management performance will continue to be critical to MC capacity

throughout and beyond the project period. Continuous improvement will be required for the production of management information and annual account preparation; production of regular cash flow statements; liability identification; and most critically, regular review of tariffs and charges and collection efficiency. To improve their financial capacity to contract loans, the MCs must (i) ensure that revenue growth is incorporated into their charging policy, and (ii) exercise discipline in formulating future expenditure plans against the background of known financial liabilities. Participating MCs will be required to report to the PCU on implementation of financial management action plans, and in the event of shortfalls, will discuss and agree on interventions necessary to achieve the original targets.

G. Environmental and Social Measures

1. Environment

92. The Project will address environmental and social issues related to identifying, preparing, and implementing subprojects, and will take steps to alleviate negative environmental and social aspects. Sample initial environmental examinations (IEEs) of selected prepared subprojects identify positive impacts on the environment. Initial environmental examinations will be prepared for all subprojects in accordance with relevant Government regulations and ADB guidelines, and documented in the subproject appraisal reports. The Environmental Protection Agency, originally located within PDD, and created in October 1992, was upgraded and made a regular attached department on 4 November 1993. The agency, headed by a director general, is responsible for enforcing environmental laws and standards across all departments and organizations within the province. In addition, an environment section was commissioned within PDD on 20 January 1992. This section is responsible for developing environmental plans and policies, and integrating environmental concerns in development planning. Environmental impact assessments of public sector projects, will be reviewed by the environment section to ensure that environmentally damaging projects are not approved. Initial environmental examinations will be prepared initially at the local government level and, if necessary, through the department for environment at the provincial level.

2. Social

93. Social measures will be incorporated into the preparation of subprojects by consulting with beneficiary groups, particularly women and the poor, CBOs, and NGOs to ensure maximum participation of such groups in subproject identification, preparation, implementation, and O&M of completed subprojects. CBOs are by far the most important community group as they generally represent low-income communities and are found in most of the urban towns. CBOs represent a community structure in low-income neighborhoods that can be tapped during project implementation. In project towns where CBOs do not exist, NGOs recruited under the Project will assist in establishing CBOs. Sample perception surveys carried out in the first-phase project towns provide an assessment of public perceptions of urban infrastructure, urban service delivery, community priorities, absorptive capacity, willingness to pay, and gender issues.

94. Each PIT, in association with NGOs and CBOs, will develop and implement a coordinated public information, education, and participation program with the participating local governments. The program, which will be sustained over the duration of the Project, will focus on (i) the proper use of the facilities; (ii) the benefits of good hygiene and public health; and (iii) community participation through a consultative process with community leaders and spokespersons, including women, to determine existing and future needs and to establish day-to-day activities for adequate O&M of public facilities.

V. PROJECT JUSTIFICATION

A. Economic and Financial Analyses

1. Analyses

95. Indicative economic internal rates of return (EIRRs) and financial internal rates of return (FIRRs) for a representative range of subprojects are shown in Appendix 14. The evaluations indicate (i) an EIRR of 17 percent for road improvements, based on savings in vehicle operating costs and personal travel time savings; (ii) an FIRR of 6 percent for sanitation improvements, based on indications of willingness to pay; (iii) an FIRR of 7 percent for solid waste, based on indications of willingness to pay and reduced O&M costs to clear drains; and (iv) an FIRR of 11 percent for improved water supply, based on increased revenue from tariffs. An analysis of the sensitivity of the results of the evaluations to changes in key variables (including a 10 percent increase in capital costs, a 10 percent reduction in benefits, a delay of one year in subproject benefits, and combinations of these changes) indicates that, with the exception of the road improvement project, the EIRRs and FIRRs fall to generally very low levels.

96. Given the subprojects' focus on public good, and the external socioeconomic and environmental benefits that will accrue from them, but which cannot be quantified fully in financial or economic terms, the EIRRs and the FIRRs of the sample subprojects indicate the potential for returns from the investments to be reasonable. In the sensitivity analysis for the subprojects, the lowest EIRR and FIRR were both 4.1 percent, with the FIRR exceeding the weighted average cost of capital of 2.5 percent incurred by the MCs to implement subprojects.

2. Financial Projections for Urban Towns

97. The seven first-phase MCs currently have positive, though modest, cash balances. The towns have generally achieved a small excess of revenue over expenditure in recent years, but all incurred a deficit in 1997/98 due to unusually large increases in expenditure. With modest reserves, the towns have limited capacity to operate deficits, and thus keep their income and expenditure broadly in balance. From 1996/97 to 1998/99, the MCs were able to undertake development expenditure that was, on average, equal to 15 percent of their total outlays. However, the modest financial turnover of the MCs resulted in total capital outlays for the seven towns of only PRs5 million per annum. Achieving a sustainable increase in investment in public infrastructure through the Project by participating MCs will require a substantial increase in their revenue to finance the incremental administrative cost of implementing subprojects, improved O&M, and eventually, debt service on subloans. This will be supported by implementation of improved accounting and financial management procedures by MCs through the municipal finance capacity building component of the Project.

3. Cost Recovery, Subsidies, and Sustainability

98. Surveys indicate only limited willingness by the community to pay for improved services (about PRs11 per household per month for improved drainage and sanitation, and PRs25 per household per month for improved water supply), despite current high levels of morbidity due to waterborne diseases. The community development and participation component of the Project is designed to increase public understanding and ownership of subprojects to improve the capacity to impose higher charges to improve cost recovery.

B. Social Dimensions

99. The urban infrastructure and community development components of the Project will improve living conditions, the local environment, and the provision of services needed by households and businesses in up to 24 MCs with a current total population of about 1.0 million. The direct beneficiaries of improvements in urban infrastructure and services include people who will gain access to new services, and people for whom existing services will be improved. In addition, indirect benefits related to improved solid waste management, environmental sanitation, and drainage will accrue to the general population living in the towns covered by the Project. The involvement of the public in subprojects will complement and reinforce the immediate economic and health benefits associated with water supply, drainage, sanitation, and solid waste management components of the Project by ensuring sustainability and ownership.

100. The incidence of waterborne diseases is high in towns, with about 80 percent of households surveyed in the initial project towns reporting that a member of the household had been ill during the month prior to the survey. Improved access to water supply and solid waste services will save time, raise public health standards, and reduce the physical burden for women and children, who are mainly responsible for carrying water and garbage. The sanitation and drainage components will raise public health standards by diverting effluent to suitable outfalls away from residential areas and by increasing the treatment of effluent. Improved health standards will reduce the number of school days and workdays lost to illness and medical expenditures. The drainage components will reduce the risk of flood damage to property, and health risks resulting from flooding and stagnant water. Road subprojects will ease traffic congestion, facilitate access and mobility, improve road safety, and reduce the level of air pollution and noise.

101. The Project will consider and address the needs of, in particular, the urban poor, women and children. The selection criteria for subprojects, and design and implementation arrangements, will ensure that subprojects are targeted to primarily benefit these groups. The community development and participation component of the Project will maximize community involvement, by both beneficiary groups and CBOs, in subproject identification, preparation, and implementation, and will increase the awareness of MC staff of their responsibilities and community expectations. This will be critical for the ultimate success of the Project and the sustainability of the benefits it delivers (Appendix 15).

102. The Project will improve the living conditions of up to 400,000 residents in about 26 urban centers and will enhance the quality of life and health, improve the environment, and create conditions conducive to sustained urban development and economic growth. The Project will contribute to a reduction in mortality, morbidity, and poverty, and the loss of amenity associated with environmental degradation in the urban centers, among all segments of the community, especially among slum inhabitants and poor groups, particularly women and children, who are estimated to make up 15 percent of the urban population. The Project will also support improvements to the capacity of local governments, improving their financial and operational management and planning, including local resource generation.

C. Impact on Poverty

103. Two notable sources of substantially increased income are the immovable property tax, which is entirely the responsibility of the NWFP government, and water charges, the rates for which are set by the NWFP government. The MCs and the NWFP government have indicated a willingness to implement actions to increase MC revenue. Immediately required actions are to (i) initiate incremental increases in water charges over the first two years of project implementation to PRs85 per household per month; (ii) identify and regularize illegal water connections; and (iii)

prepare a clear tax base for the immovable property tax, to identify potential income from the tax, and to implement a plan to significantly increase revenue from the tax, especially in MCs where current collection efficiency is below 10 percent. The real level of the water rate will need to be increased by about 5 percent per annum so that expenditure on O&M can be increased and full cost recovery for water services eventually achieved.

104. Surveys indicate only limited willingness by the community to pay for improved services despite high levels of morbidity due to waterborne diseases. Increased confidence in MC ability to deliver improved water, drainage, sanitation, and waste disposal services, and enhanced understanding of the benefits of these improvements are needed to boost the community's willingness to pay for the benefits that will accrue. The community development and participation component of the Project is designed to support this process. The potential exists to add a surcharge to water charges or the immovable property tax to recover the cost of providing improved drainage, sanitation, and waste disposal services. Specific charges can be imposed for solid waste disposal from concentrated sources of waste such as markets, commercial areas, and industrial sites.

105. Financial projections for the seven MCs initially proposed for inclusion in the Project indicate a capacity and general willingness to generate sufficient revenue to meet incremental administration and O&M costs, and debt service associated with subprojects implementation. The principal sources of additional revenue are the immovable property tax and water charges, and revenue from charges for infrastructure and services resulting from subprojects. The financial projections indicate the potential for the MCs to service subloans, with the minimum debt service coverage ratio being an acceptable 3.1. If a substantial increase in income from the immovable property tax and water charges cannot be achieved the ability for MCs to undertake improved O&M and to service subloans will be jeopardized.

106. A proposed incremental increase in the cost of water over the first two years of project implementation from PRs60 to PRs85 per household per month is expected to increase the average level of O&M costs in the seven first-phase project towns from the current 46 percent to 60 percent after allowing for an increase in O&M costs to a more adequate level. The higher rate of PRs85 per household per month is equal to 2 percent of average 25th percentile household income of PRs4,500 per household per month, which suggests that the real level of water tariffs could still be increased, while still ensuring adequate access to water by low income households. However, continuing real increases in recurrent expenditure are needed to bring O&M to a level that will enable current water supply systems to be sustained over the long term. Accordingly, full cost recovery for water supply systems is unlikely to be achievable during project implementation. However, where water meters are installed, water charges should be adjusted to achieve full cost recovery within three years; higher charges can be imposed for users of large quantities of water while ensuring that low income groups have access to water at an affordable rate.

107. The lack of a tradition of user charges for sanitation, drainage, and solid waste disposal makes it difficult to achieve full cost recovery for these services. Moreover, under ADB's policy on subsidies, moderate cost subsidy can be provided for these services because of their public good features and the positive externalities that result from their presence. User charges for solid waste collection and sanitation will be initiated for the Project, albeit at a low level initially and with real increases in charges over time as household income rises and community acceptance of the approach increases. In the meantime, the immovable property tax provides the most effective means to finance the cross-subsidy for those services where full cost recovery is not achieved; the tax is mildly progressive and is used in many countries as a means to finance urban services such as drainage and solid waste collection. This reinforces the critical need to increase the collection efficiency for the immovable property tax.

108. The public good features and the positive externalities of the subprojects justify the provision of a maximum of 80 percent of the cost of subprojects as a grant, with the MCs borrowing the remaining minimum 20 percent of the cost of the capital works of the subprojects. The NWFP government and MCs will also finance incremental administration and O&M costs for subproject implementation and debt service obligations from their own resources, supplemented by enhanced user charges. The community development, institutional development, and municipal finance capacity building assistance provided under the Project will improve financial management and community understanding; this should enable subsidies to be reduced and O&M improved, thereby ensuring project sustainability.

D. Risks

109. The major risks associated with the Project include (i) NWFP government borrowing capacity; (ii) uncertainties relating to the effective implementation of devolution of responsibilities to the local governments, (iii) limited institutional capacity of the local governments to respond to additional devolved responsibilities, and (iv) low financial capacity of the MCs resulting in fewer participating urban towns and subprojects than projected. The Project involves a significant degree of policy initiatives. It will be implemented through the local governments, and with extensive community participation to develop project ownership, leading to greater accountability at the local level. The major project risks have been minimized and will be adequately responded to by the Project.

VI. ASSURANCES

110. The Government has given the following specific assurances, in addition to the standard assurances incorporated in the legal documents.

- (i) The NWFP government, in line with the Government's devolution program (Local Government Plan 2000), will implement the time-bound Urban Sector Policy Action Plan, and will advise ADB on an annual basis of actions taken to implement the plan.
- (ii) Existing block water tariffs within the MCs will be incrementally increased over the first two years of project implementation, from the present level of PRs60 per household per month, to PRs85 per household per month, along with measures to improve collection of water charges.
- (iii) The NWFP government will agree to the full application of the immovable property tax in all participating MCs, as a condition of participation in the Project, along with an incremental increase in the existing tax base.
- (iv) The NWFP government will ensure that each participating MC will have established a PIT prior to acceptance in the Project.
- (v) Each participating MC will be required to commit a minimum of 20 percent, and up to a maximum of 50 percent, based on the MCs current and projected financial capacity at the time of subproject approval, of the total cost of the capital works of each subproject to be implemented within their respective town.
- (vi) Participating MCs will prepare management and financial action plans for their technical and financial management strengthening, which will show that they can

meet their obligations, including the cost of O&M of subprojects and debt service, to ensure long-term sustainability, as a criteria for participation in the Project.

- (vii) The federal Government will continue to accord priority to schemes and programs aimed at poverty reduction and community participation.
- (viii) The federal Government will ensure and cause the NWFP government to ensure that the PCU and MCs maintain separate accounts and reports in relation to the Project and subprojects that are to be included in the reports and accounts to be submitted to ADB.

VII. RECOMMENDATION

111. I am satisfied that the proposed loan would comply with the Articles of Agreement of the ADB and recommend that the Board approve the loan in various currencies equivalent to Special Drawing Rights 16,136,000 to the Islamic Republic of Pakistan for the North-West Frontier Province Urban Development Sector Project, with a term of 32 years, including a grace period of 8 years, and with an interest charge at the rate of 1 percent per annum during the grace period and 1.5 percent per annum thereafter, and such other terms and conditions as are substantially in accordance with those set forth in the draft Loan and Project Agreement presented to the Board.

TADAO CHINO
President

16 October 2001

APPENDIXES

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Supplementary Appendixes (available on request)

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C	Detailed Project Costs
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E	Benefit Monitoring and Evaluation
F	Summary Initial Environmental Examination
G	Financial Projections of Municipal Communities

PROJECT FRAMEWORK

Design	Targets	Monitorable Mechanisms	Risks/Assumptions
1. Sector/Area Goals			
Sustainable improvement in the environmental health and quality and life of the residents of the urban centers in the North-West Frontier Province (NWFP)	Basic infrastructure and urban services are available to support future growth and development	Consultations with Department of Local Government, Elections, and Rural Development (LGERD)	LGERD develops the institutional capacity to serve as the executing agency (EA)
		Data available from hospital records and health nongovernment organizations (NGOs)	Government adopts institutional policy reforms
	Overall health conditions improve in project towns	Consultation with urban local governments	Urban local governments demonstrate greater responsibility in municipal management
		Quarterly progress reports, review missions, and project completion report	Urban local governments enhance financial management capabilities and resource generation activities
2. Purpose /Objectives			
2.1 Improve environmental and health conditions in project towns by improving water supply, sanitation, solid waste management, roads, and drainage for low-income families.	Environmental and health conditions in project towns improve	Quarterly progress reports	Improvements in water supply, sanitation, solid waste management, roads and drainage, with improvements being well utilized with efficient operation and maintenance (O&M)
		Review missions	
		Midterm and Project Completion Report survey	
		Subproject appraisal reports	
2.2 Improve municipal management in project towns by strengthening institutional capacities and promoting policy reforms focused on greater devolution of authority.	Municipal management capacity in project towns improves and appropriate policy reform measures are instituted in support of devolution and the Urban Sector Policy Action Plan	Implementation plans and schedules	Improvements in municipal management are sustained leading to improvement in overall living conditions
		Disbursement of loan funds	
3. Components			
3.1 Institutional policy reforms along with sustainable planning and management of urban local governments	Improved governance: - Local governments to take greater responsibility for planning, coordination, and implementation of development projects (March 2001-2002)	Quarterly progress reports	Limited available qualified staff
		Review missions	No political will to implement policy reforms
		Midterm review	
		Consultation with provincial and urban local governments Consumer and staff	Staff opposition to reform program Local urban

Design	Targets	Monitorable Mechanisms	Risks/Assumptions
	<ul style="list-style-type: none"> - Improved coordination and rationalization of responsibility for urban services and management between provincial and local governments (May 2001-2002) - Review Human Resources Development requirements of local governments and provide training support (Jan 2001-2004) <p>Financial strengthening:</p> <ul style="list-style-type: none"> - Implement improved accounting , management and budgeting systems (Jan 2001 onward) - Update immovable property tax registers (July 2001) - Regularize illegal water connections and improve collection efficiency (June 2002 onward) - Increase water tariffs to PRs85 per household per month (March 2002) - Develop financial programs and tariff requirements for recovery of full O&M costs of water supply systems (Jan 2003-Jan 2004) 	<ul style="list-style-type: none"> surveys More streamlined and focused sector planning Greater accountability and responsibility at the urban local government level Greater cost recovery of urban services Improved efficiency and delivery of urban services Increase in generated revenue of local governments 	<ul style="list-style-type: none"> governments do not accept challenge of more responsibility and no improvement in municipal management and service delivery results do not improve Local urban governments do not generate sufficient financial resources to sustain investment program
3.2 Empowerment of urban communities	Community representatives are involved in the project steering committee, selection of subprojects and overall project management procedures	<ul style="list-style-type: none"> Review missions Meetings with community leaders 	<ul style="list-style-type: none"> Communities remain committed to the Project NGOs effectively develop community-based organizations, community support is positive, and strong partnerships result.

Design	Targets	Monitorable Mechanisms	Risks/Assumptions
	Community involvement in the protection and promotion of the environment and implementation of community awareness programs		
3.3 Urban Investment Programs			
a. Road improvements	Widening and upgrading of urban local government roads	Project Coordination Unit (PCU) and local government monitoring of subprojects	Timely establishment of monitoring systems and recruitment of PCU and consultants
b. Water supply improvements	Improvement to existing water supply system by installing reservoir tanks, constructing new bores, providing expanded distribution system, rehabilitating pipelines and standposts	PCU and local government monitoring of subprojects Reduction in unaccounted for water Implementation of realistic tariff structure to at least cover O&M costs PCU and local government monitoring of subprojects	Commitment of local funding from all levels of government Urban communities prepared to pay service fees and tariffs Timely preparation of subproject designs
c. Sanitation and sewerage improvements	Provision of sanitary latrines to low-income households, construction of small sewerage treatment plants and septic tanks	Improved health conditions, reduced odors and less pollution	High level of community involvement in all phases of the Project Local government participation in training programs
d. Storm-water drainage	Improvements to storm-water drainage systems through the rehabilitation of primary drains and canals, and introduction of maintenance procedures	PCU and local government monitoring of subprojects Reduction of flooding Minimization of stagnant surface waters	Greater devolution of authority to local governments and capacity of local governments to assume added responsibility
e. Solid waste management	Solid waste management improvements through the provision of waste collection and disposal equipment, development of suitable landfill sites and solid waste management training	PCU and local government monitoring of subprojects More efficient collection of solid waste Elimination of open dumping practices	Local governments undertake improved financial management and resource generation activities Continued skills upgrading of local government staff and improved management systems

Design	Targets	Monitorable Mechanisms	Risks/Assumptions
4. Activities/Inputs			
4.1 Urban Infrastructure:		Annual progress reports	The PCU and local governments will carry out contract bidding and awards in a timely manner
a. Civil works contracts and materials supply contracts:		Review missions	
		Quarterly reports	
- Water supply	\$3.5 million	Appraisal of selected subprojects	Strict supervision of implementation of subprojects will be undertaken
- Sewerage and drainage	\$9.7 million		
- Solid waste	\$2.2 million	Detailed design report	
- Roads	\$8.0 million		
b. Community development and participation	\$0.7 million	Implementation schedules and plans	Institutional support Consultants appointed in a timely manner
		Construction and procurement progress reports	The PCU will recruit consultants for capacity building, design and construction supervision, and training in a timely manner
4.2 Institutional development			
a. Implementation support	\$1.7 million	Disbursement/reimbursement of loan funds	
b. Municipal finance capacity building	\$1.2 million	Subproject completion reports	Recruitment and appointment of NGOs is done in a timely manner, and the NGOs are able to effectively develop community-based organizations
c. Incremental administration	\$2.5 million	Project completion reports	
		Annual work plans	
4.3 Interest	\$0.5 million		
4.4 Total	\$30.0 million		
	A total of 22 person-months of international and 192 person-months of domestic consulting for project management support during implementation and 14 person-months of international and 168 person-months of domestic consulting for municipal finance management support to local governments		Counterpart funds will be provided in a timely manner Municipal committees will strictly implement the financial management reforms in a timely manner

URBAN CENTERS IN NORTH-WEST FRONTIER PROVINCE

Town	Project Town	Adminis-tration	Population (1998)	Population Growth Rate, 1981-98 (% pa)	Local Government Income, 1998 (PRs/capita)
Peshawar	SUDP	MC	988,010	3.3	284
Mardan	SUDP	MC	244,510	3.0	176
Mingora	SUDP	MC	174,470	4.1	204
Kohat	SUDP	MC	125,270	2.9	259
Abbottabad	SUDP	MC	106,000	2.8	251
D.I. Khan	SUDP	MC	90,360	1.7	362
Nowshera		MC	89,430	1.1	108
Charsadda	NUPD	MC	84,260	1.8	241
Swabi	NUPD	MC	78,960	3.2	87
Shabqadar		MC	53,600	3.3	136
Mansehra	NUPD	MC	52,100	3.8	550
Takht Bai	NUPD	MC	49,250	6.0	166
Haripur	NUPD	MC	47,260	2.5	508
Bannu	SUDP	MC	46,900	0.5	688
Timargara	NUPD	MC	43,770	4.5	173
Bat Khela		MC	38,220	—	188
Khalabat		MC	33,940	2.1	202
Tank		MC	33,930	1.8	408
Havelian		MC	31,390	3.9	340
Risalpur Cantt		Cantonment	31,260	2.6	—
Pabbi		MC	30,950	5.1	182
Jahangira		MC	30,540	3.1	180
Lukki Marwat		MC	30,190	2.8	334
Topi		MC	30,140	—	183
Hangu	NUPD	MC	29,990	3.9	314
Chitral		MC	29,940	—	134
Tor Dhair		TC	27,570	—	96
Karak		MC	27,030	4.1	154
Dir		TC	24,780	—	29
Tangi		MC	24,420	1.3	167
Utmanzai		MC	24,410	1.5	85
Thall		MC	24,330	1.5	379
Zaida		MC	22,220	—	56
Aman Garh		TC	21,340	5.0	292
Nawansher		TC	19,730	1.8	161
Akora Khattak		MC	19,320	2.0	438
Kulachi		TC	18,560	1.4	149
Nawankali		TC	17,470	2.3	—
Sarai Nourang		TC	16,340	—	524
Lachi		TC	15,380	2.4	284
Paharpur		TC	14,350	3.0	266
Baffa		TC	11,650	1.2	—
Shakardara		TC	9,400	—	124
Doaba		TC	7,380	—	543
Cherat Cantt		Cantonment	2,480	4.2	—
Murree Gallies Cantt		Cantonment	310	3.9	—
Total			2,973,110	3.5	249

— not available, MC = municipal committee, NUPD = NWFP Urban Development Sector Project First-Phase Towns, SUDP = Second Urban Development Project Town Implemented under Asian Development Bank Assistance, TC = town committee.

SECTOR INSTITUTIONS

A. Introduction

1. The legal and institutional framework governing urban planning and management in Pakistan involves a broad range of federal, provincial, and local agencies. Roles and responsibilities are complex and frequently overlapping.

2. In the smaller towns in North-West Frontier Province (NWFP), the crucial shortcoming of provincial and local governments is the failure to prepare and be guided by any form of plans. Any development plan is subject to cancellation or amendment with a new administration. The concept of structure plans, reflecting national and local urban policies and acting as a guide for medium-term urban development and investment plans, is unknown, not recognized in current legislation, and generally not understood. Development control is effectively absent, making the enforcement of any policies and programmes impossible.

B. Legal Framework

1. Relevant Legislation

3. **NWFP Urban Planning Ordinance 1978.** The ordinance prescribes the establishment of a provincial urban development board (PUDB), within the Physical Planning and Housing Department (PPHD), to give, formulate, and amend long-, medium-, and short-term policies for development of NWFP urban areas (so-called development policies). PUDB is empowered to establish local area authorities (LAAs), to undertake detailed planning and implementation, including fundamental tasks of land-use planning, development control, and building control. PUDB is financed by annual development grants from the provincial government, loans from financial institutions, and profits from development activities. The ordinance permits any planning agency (PDD, PUDB, LAAs, division, district, or urban area) to adopt land development regulations.

4. **NWFP Local Government Ordinance 1979.** The ordinance describes the duties and responsibilities of local councils (LCs) and includes broad provisions for municipal committees to produce master plans and other development regulations for their urban areas, as well as building regulations. The ordinance provides for LCs to prepare development plans for selected schemes. No specific mention is made of zoning as a means of land-use planning and control, but the ordinance does assign the responsibility for the development, expansion, and improvement of an area within the municipality.

5. **PUDB Land Development Regulations, 1980.** The regulations define matters to be provided within urban development planning schemes (UDPS) and the type of UDPS. The regulations include detailed procedures for preparing schemes, and allows PUDB and LAAs to make zonal plans showing the purpose for which any areas can be primarily used.

6. **Local Council (Budget) Rules (1980).** The rules prescribe budget procedures and financial organisation to be adopted by all councils.

7. **National Reference Manual for Planning and Infrastructure Standards (1986).** The manual, produced for the then Ministry of Housing and Works, Environment and Urban Affairs Division, defines standards and targets for the provision of a wide range of (urban) services.

8. **Eighth Five Year Plan (1993–1998).** The plan provides targets relevant for urban areas

including (i) access to clean water for all; (ii) access to sewerage facilities to all urban areas; (iii) increase in tertiary roads; (iv) provision of town development schemes. A national urbanization policy followed by provincial urbanization policies and a framework for regional development of new towns will be formulated with policy implementation during the plan period.

9. **The Ninth Five-Year Plan (1998–2003).** Not yet published, an early draft gives priority to effective and increased involvement of local bodies in planning, developing and maintaining water supply and sanitation programs.

2. Procedures

10. The current sequence of procedures governing the planning and implementation of development projects within urban areas can be outlined as follows:

- (i) directive is issued by the provincial government (PDD, CM), through the chief secretary, to the respective line department;
- (ii) or an alternative until recently: proposals for investment into development projects as generated by members of national or provincial assembly (no longer active);
- (iii) the line departments prioritize the proposals;
- (iv) line department prepares project, prepares PC-I or PC-II for submission to the provincial government (PDD); and
- (v) PC-I sent to PDD for review and concept clearance, and to PDWP for approval

C. Institutional Framework

1. Provincial Government Departments

11. NWFP is divided into seven divisions, each headed by a commissioner. Each division is divided into 24 districts, controlled by deputy commissioner. Each district is divided into tehsils, presently controlled by an assistant commissioner. Within the district, certain areas are designated as urban areas, administered by a town council (either a municipal corporation (Peshawar), municipal committees, or town committees). Under the Local Government Ordinance, promulgated in August 2001, the organization of local government has been restructured into three levels: district, tehsil, and union, with devolution of power to local level governments, and the creation of district assemblies. The plan integrates the rural with the urban local governments, into one coherent structure, in which the district administration is answerable to an elected chief executive of the district. Citizen monitoring by elected representatives, the civil society's involvement with development, and a system of effective checks and balances, completes the hard core of the political structure and system of the local government.

12. The NWFP government (headed by the chief minister and the chief secretary) includes several departments (each headed by a secretary) involved with the development of urban areas. A summary of the functions and responsibilities of the main departments follows. In addition, several derived agencies and boards reporting to the main urban planning department, the PPHD, play important roles in implementing development programs, particularly those supported by international funding.

13. **Planning and Development Department.** Headed by an additional chief secretary, PDD has overall responsibility for planning and development of all sectors in the province,

including policy and procedures. It has a key role, through its coordination function, in preparing and reviewing annual budgets of the provincial annual development program (ADP). PDD reviews development investment proposals from all line departments, and prepares recommendation to the NWFP government, as part of the plan approval procedures. Most issues relevant to urban development fall under PPHD additional secretary and the respective chief.

14. **Provincial Development Working Party (PDWP).** Headed by an additional chief secretary (development), the PDWP includes secretaries of provincial departments involved with development as members. The party is responsible for reviewing project proposals for inclusion in annual plan and five-year plans. It has authority to approve provincial schemes up to PRs100 million per scheme. Projects above this value need to be approved at the federal level, by the Central Development Working Party (CDWP).

15. **Local Government, Elections, and Rural Development Department (LGERD).** LGERD is mandated to administer the NWFP Local Government Ordinance (1980). Its Local Council Board manages activities relevant to local councils and reports directly to the secretary, LGERD.

16. **Physical Planning and Housing Department.** PPHD has primary responsibility for the planning and implementation of physical infrastructure, by implementing the NWFP Urban Planning Ordinance. PPHD is responsible for land-use planning, guiding and controlling urban growth and development, and planning and implementing projects related to civic facilities. PPHD is also responsible for area development schemes, new townships, improvement of slums, utilities and urban services, and rehabilitation of public and private housing.

17. **Provincial Urban Development Board.** PUDB is a semiautonomous body, with the secretary, PPHD as its managing director. PUDB is entrusted with the formulation of policies for developing urban areas and securing compliance by government departments and agencies. PUDB has delegated part of its powers on urban development to 6-7 urban development authorities (those of Dera Ismail Khan, Hazara, Kohat, Malakand, Mardan, and Peshawar). In addition, it includes the project management unit, established to implement the Asian Development Bank-supported Second Urban Development Project.

18. **Development Authorities (DAs).** Under the legislative framework of the NWFP Urban Planning Ordinance 1980, PUDB established local development authorities (for Dera Ismail Khan, Hazara, Kohat, Malakand, Mardan, and Peshawar) to undertake detailed planning and implementation of development plans within a designated area. In practice, the DAs have been primarily involved in providing serviced land for residential, commercial, or industrial development. Infrastructure within such schemes is to be provided by the DAs, and subsequently handed over to local councils. However, frequently councils are reluctant to accept responsibility for such maintenance, as no revenue is linked with the greater operational responsibility. DAs in NWFP seem to have all but abandoned their infrastructure development role.

19. **Project Management Unit (PMU).** Established to implement the Second Urban Development Project (SUDP) and headed by a director general. The PMU was made the counterpart agency of other urban development initiatives, in particular of the Community Infrastructure Project (CIP) (supported by World Bank, Swiss Agency for Development Cooperation, and United Nations Children's Fund, as a spin-off of the Shelter for Low Income Communities Project, originally under the National Housing Authority (NHA). The PMU is now divided into two units, for the SUDP and for CIP.

20. **Public Health Engineering Department (PHED).** PHED is responsible for the development of water supply systems in urban and rural areas. Once completed, urban water supply schemes are usually handed over to the municipal committees (MCs) for operation and maintenance. PHED prescribes water tariffs. Currently, PHED in collaboration with Kreditanstalt für Wiederaufbau is experimenting with installing water meters in selected (small) towns (Baffa, Kulachi, Lachi, Nawan Killi, Nawan Shaher, Thal, and 11 villages). Setting metered water rates is the responsibility of the local council managing the system.

21. **Communication and Works Department (CWD).** CWD's main relevance for urban infrastructure and services is its mandate to construct, repair, operate, and maintain provincial roads (and associated roadside drains), bridges, and tunnels in the province. It is often contracted by the National Highways Authority (NHA) to maintain sections of the national highway network. Urban roads are the responsibility of local councils, although this may also be subcontracted to CWD for practical purposes.

22. **Water and Power Development Authority (WAPDA).** This is a national institution, with provincial delegations, with a board responsible for the provincial area. In addition to its responsibilities in managing national water resources, WAPDA generates, transmits, and distributes electric power to households. WAPDA is responsible for reading meters and billing consumers.

23. **Sui Northern Gas Pakistan Ltd.** This company is responsible for transmission and distribution of natural gas to householders; an increasing number of NWFP towns are getting connected with individual metered gas connections.

24. **Cantonment Board.** Part of the Pakistan Army, a cantonment board is responsible for planning, developing, and maintaining urban infrastructure, services, and civic amenities such as health and schools. Currently, there are nine boards in NWFP. A cantonment board can be opened or closed according to the defence needs of the country.

2. Urban Local Government

25. Urban local government in Pakistan was provided by local councils administered by the Local Council Board (LCB) within LGERD. Local councils include the Peshawar Municipal Corporation, 29 MCs, and 16 town committees. All project towns are classed as MCs. MCs are classified in categories, depending on the level of revenue¹ (Class A: >PRs15 million; Class B: between PRs5 million and PRs15 million) and Class C (< PRs5 million). No direct correlation exists between these categories and the size of the urban population. Staffing levels as assigned by LCB are a function of category, not of urban population.

26. The MCs have a range of mandated functions, compulsory and optional. In addition to the provision of basic urban services and infrastructure, the MCs are also responsible for drawing up master plans and site development plans, and a form of building control. MCs are, with some exceptions, short of skilled staff, and do not have adequate local revenue. Maintenance of urban infrastructure is given low priority. Urban populations have little confidence in local government, and are reluctant to pay existing taxes and charges.

27. Elections for local councils were suspended in 1996, and towns have been administered by an administrator, appointed by the secretary, LGERD. The administrator is supported by officers heading four main departments. The main MC departments relevant to urban services

¹ Definition of revenues categories before the abolition of octroi.

and infrastructure are (i) health department: responsible for sanitation (primarily solid waste management (on average 78 percent of budget in project towns), drainage (21 percent), and vaccination (<1 percent)); (ii) water supply department: responsible for water supply, firefighting, and street watering; (iii) building and works department: responsible for roads, general municipal works, building control, gardens, roadsides, and street lighting. Table A3 provides an overview of the allocation of responsibilities in urban planning and management for various sectors. With the promulgation of the Local Government Ordinance in August 2001, the administrative system is being changed, with the replacement of the administrator by a duly elected council representing all segments of the community. However, the existing infrastructure and service delivery departments will remain, with changes only in their laws, rules, and regulations.

Table A3: Allocation of Urban Planning and Management Responsibility

Sector	Planning & Design	Implementation / enforcement	Operation & maintenance
Preparation of structure plans	PPHD; through LAAs	PPHD	Not applicable
Development control	PPHD	PPHD	Not applicable
Land management	PPHD	PPHD	Not applicable
Water supply	PHED	PHED	MC – Water supply department
Drainage	MC – Health Department	MC – Health Department	MC – Health Department
Sewerage / sanitation	MC – Health Department	MC – Health Department	MC – Health Department
Solid waste management	MC – Health Department	MC – Health Department	MC – Health Department
Roads & access:			
National	NHA	NHA / CWD	CWD
Local	MC – Building & Works Department	MC	MC
Electricity	WAPDA	WAPDA	WAPDA
Gas	SNGPL	SNGPL	SNGPL
Fire	MC	MC	MC

CWD = Communication and Works Department, LAA = local area authorities, MC = municipal committees, NHA = National Highways Authority, PHED = Public Health Engineering Department, PPHD = Physical Planning and Housing Department, SNGPL = Sui Northern Gas Pakistan Ltd., WAPDA = Water and Power Development Authority.

EXISTING INFRASTRUCTURE AND SERVICES IN URBAN TOWN

A. Introduction

1. Information about the quality and extent of the existing infrastructure and services in urban areas in North-West Frontier Province (NWFP), and the seven phase 1 towns (the project towns) in particular, is mainly drawn from Asian Development Bank (ADB) technical assistance (TA), namely Urban Infrastructure Needs Assessment,¹ and NWFP Urban Development Project.² These studies concerned larger towns, thus the quality of service in the remaining (smaller, more remote) towns in NWFP will be less than described in this section. Responsibility for the installation or construction, operation, and maintenance of infrastructure covers a number of provincial and local government agencies, as well as individual households. Table A4 provides a summary of quantitative data on the provision of infrastructure and services in the seven first-phase project towns.

B. Infrastructure Sectors

1. Water Supply

2. The provision of piped water supply in the project towns at present ranges from 25-83 percent of urban households. Takht Bhai and Swabi have only 8 percent coverage, due to the noncommissioning of existing Public Health and Engineering Department (PHED) schemes. The figures hide a wide range of quality differences, with hours of service per day as low as 1-3 hours. Community taps (standpipes) are not common in NWFP, with a maximum of 6 percent (Charsadda, Mansehra) of the population dependent on such taps as their main source of water.

3. PHED is usually responsible for the major part of the design and construction of water supply schemes, from source development, treatment, transmission, storage, and primary and secondary distribution. Tertiary distribution and house connections are the responsibility of the local council. Upon completion, the scheme is handed over to the local councils for operation and maintenance. Billing is also the responsibility of local councils, although at rates set by PHED. Water meters have not yet been introduced in the project towns, but a Kreditanstalt für Wiederaufbau supported program of meter installation is under way elsewhere in urban NWFP. Scheme designs usually follow a standard design, without a great deal of site-specific detail. Capacity of tubewells, reservoirs, and transmission mains follows standard designs.

4. The fundamental problem with most piped water supply schemes is the high incidence of leakage (from the distribution system), wastage (water wasted from house connections through faulty fittings, continuously open taps, and overflowing house reservoirs), and illegal connections, leading to low system pressures and low water quality. Hours of operation are often severely limited (down to two or three hours per day), sometimes to reduce the high electricity costs of running tubewells. Discontinuous supply not only leads to low system pressure and thereby allowing entry of polluted water into the system, but also encourages consumers to leave their taps open for when the water returns, leading to high wastage. Alternative supply to the piped supply usually consists of wells, for as much as 70 percent of households. Most wells are open shallow wells, with water drawn using buckets. Only Charsadda has a significant (20 percent) portion of the population using wells with handpumps.

1 TA 1249-PAK: *Urban Infrastructure Needs Assessment*, for \$600,000, approved on 19 December 1989.

2 TA 2940-PAK: *North-West Frontier Urban Development Project*, for \$950,000, approved on 12 December 1997.

2. Storm-Water Drainage

5. The central problem of the degradation of the living environment in all towns is related to the condition of the secondary and tertiary drainage system, which invariably also function for carrying fecal waste. All storm-water drains are contaminated with wastewater and are effectively open sewers. Surveys (1993) show that the majority of drains in the project towns are lined, with roughly 25 percent in good condition, the remainder in average or poor condition. Even lined drains may not function adequately as they are seldom part of an interconnected network, with adequate slope and profile. Maintenance of the drainage network is the MC's responsibility. Performance on drainage maintenance varies, but is generally poor.

3. Sewerage and Sanitation

6. None of the project towns have piped sewerage. The majority of households are reported to have a septic tank, although the definition of a septic tank and simple cesspit with or without a soakpit is not clear. Survey data are therefore not consistent. Septic tanks in town centers are old and not designed to present standards, i.e., with two or three chambers. None of the local councils in any of the towns offer a septic tank desludging service. Thus, septic tanks do not offer any form of treatment and the effluent quality is little better than that of raw sewage. A significant percentage of households (as high as 75 percent in some towns) still practice unacceptable human waste disposal methods (open air, bucket latrine, drain).

4. Solid Waste

7. Coverage for the collection and disposal of domestic and commercial solid waste in the project towns ranges from 2-50 percent, typical coverage is around 25 percent. Collection can be from individual households or from strategic locations such as neighborhood collection points. These figures do not provide an indication of the adequacy of the disposal methods of the waste. Final disposal is generally as simple as dumping in low-lying areas, without subsequent compaction or coverage. A major problem is the reluctance of the population to pay charges for solid waste management services, which therefore remains seriously underfunded. The volume of domestic waste generated is still relatively low, as a result of limited cash economy in the smaller towns of NWFP. No specialized services exist for the disposal or treatment of special waste such as hospital waste.

5. Roads

8. Major roads (national and provincial network) are maintained by Communication and Works Department; the national roads by National Highways Authority. These are generally in good condition, with widths of 7 meters. Local roads and access roads in urban areas, and associated roadside drains, are the responsibility of the local council. The network is generally adequate in coverage, but poor in terms of road pavement quality and maintenance condition. Many roads are still unpaved, without adequate drainage, with wastewater over the road surface. In old town centers, access is often via narrow lanes, not suitable for vehicular access.

9. Traffic problems exist in most town centers, largely the result of encroachment of commercial activities and uncontrolled parking. Another aspect of traffic is the wide disparity in vehicle speed and acceleration, with the still widespread use of human or animal traction.

Table A4: Existing Infrastructure - Quantitative Data

Item	Unit	Charsadda	Hangu	Haripur	Mansehra	Swabi	Takht Bhai	Timagara	Province (46 towns)
1. Population									
Town									
1981	persons	62,530	15,530	31,120	27,840	46,340	18,330	20,870	1,659,763
1998	persons	84,260	29,990	47,260	52,100	78,960	49,250	43,770	2,973,110
2008 (forecast)	persons	100,260	43,840	60,250	73,330	119,810	86,660	67,300	4,165,193
Growth rate									
1981-1998	% pa	1.8%	3.9%	2.5%	3.8%	3.2%	6.0%	4.5%	3.5%
1998-2008	% pa	1.8%	3.9%	2.5%	3.5%	4.3%	5.8%	4.4%	3.4%
Gender ratio	female/100 male	92	93	90	95	98	93	90	89
Households (1998)	number	11,096	3,801	7,177	7,726	10,455	5,586	4,723	261,550
Av. household size in 1998	persons	7.6	7.9	6.6	6.7	7.6	8.8	9.3	11.4
Town with surrounding settlements									
1998	persons	na	33,450	59,450	54,670	87,190	54,010	na	na
2008	persons	na	49,250	75,710	79,210	130,890	95,080	na	na
District urban population	persons	186,680	61,690	81,200	63,750	176,370	293,760	43,770	na
2. Urban area (1998)									
Total land area	ha	1,201	538	984	1,008	1,109	1,339	684	35,626
Built-up area	ha	455	220	253	198	220	183	139	8,637
Estimated net density in built-up area:	persons/ha	167	123	168	237	323	242	283	310
3. Housing (1998)									
Housing stock	number	10,867	3,475	7,680	6,805	11,572	7,003	3,923	261,550
Katcha and temporary housing	% of total	26%	17%	2%	3%	19%	25%	39%	18%
4. Water Supply (1999)									
Household connections	number	2,774	1,300	5,957	4,481	836	447	2,645	95,540
Household connections	% of hh	26%	37%	78%	66%	7%	6%	67%	37%
Community tap	% of hh	6%	1%	1%	6%	0%	0%	0%	2%
Open well	% of hh	26%	60%	0%	0%	60%	73%	0%	31%
Well with pump	% of hh	20%	2%	0%	5%	2%	6%	1%	6%
Other	% of hh	22%	0%	21%	23%	31%	15%	32%	24%
5. Sanitation									
Toilet with water flush + septic tank	% of hh	45%	34%	30%	65%	30%	25%	50%	40%
1993 data:									
Septic tank	% of hh	36%	55%	76%	63%	28%	25%	50%	
Bucket latrine	% of hh	28%	19%	2%	3%	35%	23%	8%	
Open air	% of hh	22%	15%	5%	19%	32%	43%	32%	
Drains	% of hh	15%	11%	18%	14%	5%	8%	10%	
Unacceptable, total	% of hh	64%	45%	24%	37%	72%	75%	50%	
6. Drainage (1993)									
Lined drain along house	% of hh	79%	68%	77%	64%	61%	58%	28%	
Earth drain along house	% of hh	17%	21%	12%	15%	24%	38%	29%	
No drain along house	% of hh	4%	11%	11%	21%	15%	4%	43%	

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Item	Unit	Charsadda	Hangu	Haripur	Mansehra	Swabi	Takht Bhai	Timagara	Province (46 towns)
7. Solid Waste Disposal									
Regular collection	% of hh	39%	35%	29%	50%	15%	2%	12%	27%
Disposal on roads	% of hh	8%	5%	5%	10%	4%	5%	5%	6%
Disposal on open land	% of hh	52%	60%	51%	25%	81%	91%	75%	61%
Disposal in drains or river	% of hh	1%	0%	15%	15%	0%	2%	8%	6%
8. Roads									
Total length	km	98.7	43.4	70.9	57.0	59.7	54.2	51.5	2,252.2
Related to population	meter/capita	1.2	1.4	1.5	1.1	0.8	1.1	1.2	0.8
Related to area	meter/ha	82	81	72	57	54	40	75	63
Major and main roads	% of total	21%	33%	39%	42%	23%	25%	52%	32%
Local and access roads	% of total	79%	67%	61%	58%	77%	75%	48%	68%
<i>1993 data:</i>									
Roads > 3.7m									
Total length, paved	km	31.1	13.3	15.8	10	14.4	18.43	7.3	
Related to population	meter/capita	0.4	0.4	0.3	0.2	0.2	0.4	0.2	
Total length, unpaved	km	5.4	1.7	5.3	0	19.25	0	0.4	
Fraction unpaved	%	15%	11%	25%	0%	57%	0%	5%	
Streets < 3.7 m									
Total length, paved	km	27	22.15	33.4	26	15.5	12.54	3.6	
Related to population	meter/capita	0.3	0.7	0.7	0.5	0.2	0.3	0.1	
Total length, unpaved	km	19.6	4.3	0	3.4	4.7	15.1	10.6	
Fraction unpaved	%	42%	16%	0%	12%	23%	55%	75%	
Total length of roads	km	83.1	41.45	54.5	39.4	53.85	46.07	21.9	
Change from 1993 to 1999	%	19%	5%	30%	45%	11%	18%	135%	

URBAN SECTOR POLICY ACTION PLAN

Policy Objectives / Tasks	Action by (agency)	Date
1. Improve governance		
<ul style="list-style-type: none"> • Devolve greater authority and responsibility for municipal management to local government. 	<ul style="list-style-type: none"> • Federal Government, PDD, LGERD, LCB 	Aug 2000 - continuing
<ul style="list-style-type: none"> • Increase involvement of local government in planning, coordination, and implementation of development projects. 	<ul style="list-style-type: none"> • LGERD to formulate guidelines and procedures 	Mar 2002-2003
<ul style="list-style-type: none"> • Improve institutional capacity for fiscal and town management. 	<ul style="list-style-type: none"> • LGERD to provide guidance to local government 	Mar 2002-2003
<ul style="list-style-type: none"> • Improve coordination and rationalization of responsibility for urban services and management between provincial and local governments. 	<ul style="list-style-type: none"> • PDD to take lead and to formulate guidelines and procedures • LGERD and local governments to implement, monitor, and report 	May 2002-2003
<ul style="list-style-type: none"> • Increase involvement of communities, CBOs, and NGOs in planning, implementation, and management of subprojects. 	<ul style="list-style-type: none"> • LCB, local governments, and local communities 	ongoing
<ul style="list-style-type: none"> • Identify areas in which local governments need strengthening of their existing staffing capacities, and provide training support. 	<ul style="list-style-type: none"> • LGERD, LCB, and local governments 	Jan 2002-2005
2. Provide financial strengthening and resource mobilization		
<ul style="list-style-type: none"> • Implement improved accounting, management information, and budgeting systems in local government. 	<ul style="list-style-type: none"> • PDD, DOF, LGERD, LCB to evaluate procedures, recommend approach, and prepare action plan • Implementation by local governments with support from provincial government departments 	Jan 2002 – continuing
<ul style="list-style-type: none"> • Update immovable property tax registers, identify potential tax revenue, and prepare time-bound action plan for improved collection efficiency and increased revenue by local councils. 	<ul style="list-style-type: none"> • DOF 	July 2002
<ul style="list-style-type: none"> • Identify and regularize illegal water connections, and prepare a time-bound action plan for improved collection efficiency and increased revenue by local councils. 	<ul style="list-style-type: none"> • Local governments to implement • LCB to monitor 	June 2003 - continuing
<ul style="list-style-type: none"> • Increase water tariffs to improve cost recovery. Increase to PRs85 per household per month by March 2002, and review annually thereafter. 	<ul style="list-style-type: none"> • LGERD, LCB 	Mar 2003 – continuing
<ul style="list-style-type: none"> • Develop financial programs and tariff requirements for recovery of full O&M costs of existing and improved water supply systems within urban centers. 	<ul style="list-style-type: none"> • PHED, LGERD, LCB, Local governments 	Jan 2004-2005

Policy Objectives / Tasks	Action by (agency)	Date
<ul style="list-style-type: none"> Local government to consider introducing fees for solid waste and sanitation services where appropriate to recover the cost of providing services. 	<ul style="list-style-type: none"> Local governments 	Mar 2003 - continuing
<ul style="list-style-type: none"> Train local government staff in improved financial management. 	<ul style="list-style-type: none"> LGGERD, LCB 	June 2002 - continuing
3. Focus on urban services for the poor		
<ul style="list-style-type: none"> Develop indicators and monitor social and economic benefits of services to the urban poor. 	<ul style="list-style-type: none"> LGGERD and LCB to develop Local government to implement 	Sept 2002
<ul style="list-style-type: none"> Train local government staff on their role in improving and providing more equitable delivery of basic urban services. 	<ul style="list-style-type: none"> LGGERD and LCB to develop and present training programs 	Sept 2001- continuing
<ul style="list-style-type: none"> Establish and maintain channels of communication with local communities to develop priorities and for future O&M. 	<ul style="list-style-type: none"> Local governments, under guidance of LGGERD and LCB, using nongovernment organizations as intermediary where required 	July 2002- continuing
<ul style="list-style-type: none"> Train local government staff in participatory planning. 	<ul style="list-style-type: none"> Local governments, under guidance of LGGERD, LDC, using nongovernment organizations and community-based organizations 	Sept 2002 - continuing
4. Improve operation and maintenance, and rehabilitation capability		
<ul style="list-style-type: none"> Establish procedures to assess O&M and rehabilitation needs (financial, technical, human resource and equipment), and implement. 	<ul style="list-style-type: none"> LGGERD, LCB, other affected provincial departments and local governments 	Jan 2004 - continuing
<ul style="list-style-type: none"> Prepare an O&M and rehabilitation program for all municipal assets. 	<ul style="list-style-type: none"> Local governments 	Jan 2005 - continuing
<ul style="list-style-type: none"> Incorporate improved O&M budgeting into new accounting and management procedures. 	<ul style="list-style-type: none"> Local governments 	Mar 2005 - continuing
5. Provide environmental protection		
<ul style="list-style-type: none"> Undertake environmental impact assessments for all municipal infrastructure developments. 	<ul style="list-style-type: none"> PDD, EPA, LGGERD, LCB, and local governments 	Mar 2002 - continuing
<ul style="list-style-type: none"> Identify environmentally sensitive areas in towns, particularly for water sources, and ensure that development does not negatively impact on natural resources. 	<ul style="list-style-type: none"> Local governments LCB to monitor 	Mar 2003-2005
<ul style="list-style-type: none"> Involve communities in protecting and promoting the environment, and in implementing community awareness programs. 	<ul style="list-style-type: none"> Local governments, with nongovernment and community-based organizations 	Sept 2002 - continuing

CBO = community-based organization, DOF = Department of Finance, EPA = Environmental Protection Agency, LCB = Local Council Board, LGGERD = Local Government, Elections and Rural Development, NGO = nongovernment organization, O&M = operation and maintenance, PDD = Planning and Development Department, PHED = Public Health Engineering Department.

URBAN SECTOR PUBLIC INVESTMENT NEED

**Table A6.1: Urban Public Infrastructure Development Expenditure in North-West Frontier Province
(PRs million, current prices)^a**

Item	1997	1998	1999
A. Capital Expenditure			
1. Municipal and Town Committees			
Community Infrastructure Projects	5.7	1.7	0.2
Other Urban Investment	66.2	70.9	87.4
Subtotal (1)	71.9	72.6	87.6
2. North-West Frontier Province ^b	0.0	0.0	322.0
Subtotal (A)	71.9	72.6	409.6
Total by Municipal and Town Committees (Prs/capita)	25	24	28
B. Source of Funds			
1. Municipal and Town Committees	67.7	64.4	77.0
2. Higher Levels of Government	4.3	8.2	332.7
Subtotal (B)	71.9	72.6	409.6
Total			

- = not available

^a Excludes direct expenditure by the federal Government.

^b Budget specified as being for investment in urban infrastructure, but may include other items such as staff and maintenance.

Table A6.2: Estimated Cost of Upgrading and Expanding Infrastructure, 2001-2005 (1999 prices)

Item	North-West Frontier Province Urban Development Project First-Phase Towns							North-West Frontier Province (46 towns)		
	Charsadda	Hangu	Haripur	Mansehra	Swabi	Takht Bai	Timargara	Total	Total	Share
A. Investment Need (PRs million)										
1. Accrued Maintenance										
Water Supply	13.8	7.9	13.4	12.6	6.9	7.0	10.0	71.6	550	3%
Sanitation	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0	0%
Solid Waste	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0	0%
Roads and Drainage	126.8	27.0	125.2	76.2	78.9	95.0	22.1	551.2	4,250	23%
Subtotal (1)	140.5	35.0	138.6	88.8	85.8	102.1	32.1	662.8	4,800	26%
2. Expanded Infrastructure										
Water Supply	116.9	44.5	29.5	49.0	79.4	105.5	54.6	479.4	3,700	20%
Sanitation	121.4	44.8	69.3	125.7	92.4	35.6	34.1	523.4	4,040	22%
Solid Waste	39.6	17.3	23.2	26.4	40.8	29.0	22.6	198.9	1,530	8%
Roads and Drainage	55.1	24.1	187.6	71.9	79.7	39.4	129.1	586.8	4,520	24%
Subtotal (2)	333.0	130.6	309.6	273.0	292.2	209.5	240.5	1,788.5	13,790	74%
3. Total										
Water Supply	130.7	52.4	42.9	61.6	86.3	112.5	64.6	551.0	4,250	23%
Sanitation	121.4	44.8	69.3	125.7	92.4	35.6	34.1	523.4	4,040	22%
Solid Waste	39.6	17.3	23.2	26.4	40.8	29.0	22.6	198.9	1,530	8%
Roads and Drainage	181.9	51.1	312.8	148.1	158.6	134.4	151.2	1,138.0	8,770	47%
Total	473.5	165.6	448.2	361.8	378.0	311.5	272.6	2,411.3	18,590	100%
B. Average Annual Funding Deficiency										
Total (PRs million/year)										
Investment Need	94.7	33.1	89.6	72.4	75.6	62.3	54.5	482.3	3,098	100%
Local Financing Capacity ^c	3.7	1.2	6.3	3.0	0.4	1.1	0.1	15.8	405	13%
Funding Deficiency	91.0	31.9	83.3	69.4	75.2	61.2	54.5	466.4	2,693	87%
Total (PRs/capita/year)										
Investment Need	1,003	860	1,617	1,109	727	869	937	989	835	100%
Local Financing Capacity ^c	39	32	113	45	4	16	1	32	109	13%
Funding Deficiency	964	827	1,504	1,063	723	853	936	957	725	87%

^a Investment to restore current infrastructure to an adequate standard.

^b Investment to provide services for population growth.

^c Based on average annual investment by municipal committees during 1996/97-1998/99.

EXTERNAL ASSISTANCE TO THE URBAN SECTOR^a

Description	Amount (\$ million)	Approved
A. Loans		
1. Asian Development Bank		
Loan 793-PAK(SF): Karachi Urban Development	55.20	October 1986
Loan 1001-PAK(SF)/1002-PAK:Karachi Sewerage	85.00	December 1989
Loan 1004-PAK(SF): Second Urban Development	66.00	December 1989
2. The World Bank		
Lahore Urban Development	16.00	1982
Karachi Special Development	70.00	1987
Punjab Urban Development	90.00	1988
Community Infrastructure Project ^b	21.50	1994
3. The Netherlands		
Quetta Sewerage and Sanitation	12.00	1987
B. Technical Assistance (TA)		
Asian Development Bank		
TA 943-PAK: Second Urban Development	0.35	January 1988
TA 1248-PAK: Urban Financial Management and Accounting Project Pakistan	0.70	December 1989
TA 1762-PAK: Third Urban Development	0.60	October 1992
TA 2106-PAK: Institutional Strengthening of PHED in Punjab and NWFP	0.52	June 1994
TA 2639-PAK: Urban Institutional Strengthening	0.10	September 1996
TA 2940-PAK: NWFP Urban Development	1.15	December 1997
TA 3124-PAK: Urban Sector Strategy	0.15	December 1998

NWFP = North-West Frontier, PAK = Pakistan, PHED = Public Health Engineering Department,

^a Water supply and sanitation loans and TAs have not been included in the table.

^b Funding was also provided by the Swiss Agency for Development and Cooperation and United Nations Children's Fund

LESSONS LEARNED

A. Introduction

1. The Asian Development Bank (ADB) has had limited involvement in the urban sector in Pakistan, with only four projects¹ implemented and completed in North-West Frontier Province. In general, portfolio performance has been constrained by a number of generic macro and micro issues, including (i) legal and administrative issues relating to processing procedures and requirements, (ii) coordination and procedural issues, and (iii) counterpart fund constraints and timely release. These issues resulted in implementation delays, with often negative financial and economic consequences, as well as noncompliance with specific covenants, delays in consultant recruitment, minimal beneficiary participation, poor operation and maintenance of completed facilities, and limited institutional capacity. The following information provides specific lessons learned on Pakistan urban projects.

1. Karachi Urban Development Project

2. Urban upgrading is complex in nature; a piecemeal approach to a few selected problems is not an optimal solution. Urban upgrading should be designed from a plan that integrates all aspects of urban infrastructure, and involves the participation of the ultimate beneficiaries: The institutional capacity to implement the project must be present, and the financial framework must be in place to ensure long-term sustainability of the upgrading. The absence of any one of these elements will eliminate any chance for project success.

3. The implementation schedule of integrated urban development projects in megacities like Karachi should be realistic and provide adequate time allowance for staff training for new executing agencies, as well as for stoppages from unforeseen exigencies as peace and security problems.

4. When a major outstanding problem is identified at appraisal, its resolution should be a precondition for loan negotiations or at least for Board consideration. Otherwise, it could lead to suspension of contract awards, which inevitably delays project implementation.

5. The upgrading of sewerage treatment capacity needs to be synchronized with inflow of sewage available for treatment. Future financing of sewerage treatment plants should ensure that properly connected sewers deliver an adequate level of sewage for treatment upon completion.

6. The main weakness of Karachi Urban Development Project was its design. This was a direct result of the absence of project preparatory technical assistance (TA) early in the design stage of this complex undertaking. A TA would have identified the institutional shortcomings of the executing agencies, provided estimates of willingness to pay of katchi abadi residents for leases, and provided appropriate designs for the physical components of the project. Moreover, the results of such a TA would have

¹ Loan 793-PAK(SF): *Karachi Urban Development Project*, for \$55.2 million, approved on 14 October 1986; Loan 1001-PAK(SF) and 1002-PAK: *Karachi Sewerage Project*, for \$85.0 million, approved on 14 December 1989; and Loan 1004-PAK(SF): *Second Urban Development Project*, for \$66.0 million, approved on 14 December 1989.

been available for discussion with the beneficiaries and other project stakeholders, thus increasing project ownership during the design stage and the chances of its success.

7. In December 1999, ADB conducted a project performance and audit report and concluded that the project was unsuccessful. The project did not meet its original objectives. The main identified weakness was in Project design. In addition, the long implementation delays resulted from some major issues that should have been resolved prior to implementation, especially the financial solvency of the implementing agencies, which ultimately impacted on the sustainability of the project components.

8. ADB's project administration needs to be strengthened, particularly for monitoring financial and institutional aspects of a project. Loan covenants must be closely monitored and enforced during implementation. Financial covenants need to be more precise in their intentions. Weak and vague covenants tend to not be complied with, resulting in little institutional reform. Moreover, financial covenants should be based on a firm economic rationale. In the case of cost recovery, a clear relationship should exist between the beneficiary of a service and the ultimate payer for the service. This is not the case for solid waste disposal and sewage services. Because of the large positive externalities generated by these services, consideration should be given to financing these services out of general revenues.

2. Karachi Sewerage Project

9. The appraisal cost estimates for the Karachi Sewerage Project were based on preliminary designs and the Sindh government's standard unit rates, which led to cost escalation at tendering. This factor combined with the withholding of contract awards and nonavailability of part of the land for the Mauripur sewerage treatment plant led to a need to reformulate the plant layout and downsize the project. This experience underlines the need to complete detailed design, use a reliable cost base, and obtain possession of key project sites before loan approval.

10. When reformulation leads to significant scope reduction of a project, then the dimensions and the expected benefit stream of the revised project should be clearly indicated. Absence of relevant information leads to difficulties in evaluating completion and measuring benefits.

11. Beneficiary participation was limited during project implementation as it was not envisaged at appraisal. This has led to some dissatisfaction among residents in one locality served by the project. The Karachi Water and Sewerage Board (KWSB) now recognizes the importance of beneficiary involvement and has made serious efforts to accommodate beneficiary concerns in the Korangi Wastewater Management Project.

12. Given the continued need for large investments to meet growing demands for water and sewerage services in Karachi, KWSB has recognized the need for private sector participation in its activities. However, the process is tied up in a legal stalemate. KWSB needs to seek innovative solutions to this stalemate.

3. Second Urban Development Project

13. While this loan was closed on 31 December 1999, no project completion report has been completed, and no formal assessment of project performance and associated problems and issues relating to its implementation. However, a number of issues can be readily identified from the project: (i) delays in land acquisition, (ii) minimal community involvement in the project, (iii) lack of ownership by the municipal and town committees in the project towns, (iv) limited financial contribution by the towns, (v) lack of counterpart budget and untimely release, (vi) delay in consultant recruitment, (vii) frequent turnover of senior staff of the Project Management Unit, particularly at the position of director general, and (viii) limited implementation of institutional reforms. While the Project can be considered a success in so far as it implemented significant capital works subprojects, concern is noted at the capacity of the Project towns in operating and maintaining the assets, due to lack of budget and limited institutional capacity, as well as the financial capacity of the Project towns to meet their debt service obligations under the various subsidiary loan agreements. The design of the Project could be considered over ambitious considering the financial capacities of the participating towns.

B. Incorporating Lessons Learned to Project Design

14. The lessons from the experience of the previous urban projects undertaken in Pakistan have been incorporated into the project design to minimize recurrence of past problems and issues. Particular emphasis has been given to assessing the financial and institutional capacities of the towns that are likely to participate in the Project. In addition, the proposed subprojects will be small and use least-cost design solutions. The maximum amount of any subproject will be PRs50 million. Community participation will be a focus. Without the participation of community-based organizations throughout the whole project cycle, long-term sustainability will be jeopardized. Institutional strengthening of the local government units, where the Project will be implemented, has been given priority, particularly to financial management and resource mobilization. Ownership at the local government level must be a focal point of any urban project, and this aspect has been carefully incorporated into the project design. The participating towns will be required to nominate a core group of staff to be involved in project implementation, with this core group forming the basis for a permanent urban unit within the respective municipal committee. In addition, an equity share of a minimum of 20 percent for each subproject, and up to a maximum of 50 percent, depending on the MCs financial capability, will be required from each participating town. The Project will support the Government's devolution initiatives and poverty reduction programs.

SUMMARY DESCRIPTION OF PREPARED SUBPROJECTS FOR THE URBAN INFRASTRUCTURE IMPROVEMENT COMPONENT

1. The urban infrastructure component consists of town-specific investment in one or more infrastructure subprojects. The infrastructure subprojects include five different categories. Subproject appraisal studies were conducted for priority projects in the phase 1 project towns: Charsadda, Hangu, Haripur, Mansehra, Swabi, Takht Bhai, and Timargara. Details of these subprojects are summarized in Table A9. Details of some of those subprojects have been revised to reflect the commitment to basic needs and poverty reduction type subprojects, and to match both financial and institutional capabilities.

A. Water Supply Subprojects

2. While statistics on percentage of the population connected to piped water supply systems in North-West Frontier Province (NWFP) towns may seem high, the performance of the schemes is often poor, with the main deficiencies including high leakage, low pressure, many illegal connections, and very limited hours of service. Strategies are aimed at reducing the incidence of unaccounted for water and illegal connections. Subprojects will be designed to improve the quality of the service provided by existing schemes, and simultaneously increasing revenues through a combination of leak-detection programs and the conversion of illegal connections to registered accounts. These measures should improve system pressures and the quality of the water as supplied. Where necessary, distribution systems will be extended to or improved for poorly served areas. Priority will be given to servicing low-income areas.

3. Consideration will be given to installing water meters in towns that have achieved a secure 24-hour supply system, and that can demonstrate the technical and management discipline required to run a meter-based billing system. Lessons will be learned from the experience gained on the KfW-supported program of installing water meters now under way in Baffa, Kulachi, Lachi, Nawan Killi, Nawan Shaher, Thal, and 11 villages.

B. Sewerage and Sanitation Subprojects

4. The construction of full piped sewerage schemes with treatment is unlikely to be affordable or manageable in project areas. Targets are therefore aimed at improving the disposal of human waste by increasing the use of small sewerage schemes with local treatment, encouraging the installation of adequately designed individual and communal septic tanks, and improving the maintenance of these tanks by introducing septic tank maintenance services. Whether this service will be operated by the municipal committee (MC) or contracted out to a private operator will depend on the capacity of the respective MC, and realistic projections on the potential revenue resulting from service charges. The drainage component, as described in the following section, will also contribute to improving sanitary conditions as most storm-water drains are currently contaminated with human waste.

C. Drainage Subprojects

5. The central problem of the degradation of the living environment in all towns is related to the condition of the secondary and tertiary drainage systems, which invariably also carry fecal waste. Improvement subprojects are aimed at routine cleaning and rehabilitating existing systems, with particular emphasis on interconnecting isolated stretches of drainage channels into a full network. Priority areas will be high-density, low-income areas, where interventions should result in marked improvement of living conditions. Investments in new works will focus on establishing drainage networks including suitable outfalls. Drainage subprojects will all

include setting up maintenance procedures and systems, where necessary supported by the provision of (manual) equipment for channel clearing.

D. Solid Waste Management Subprojects

6. The collection and disposal of solid waste is recognized as one of the first responsibilities of fledgling local authorities. However, current reluctance of the urban population in small towns in NWFP to pay all but minimal charges for a municipal waste collection service means that system improvements must be low cost. Waste volumes generated are relatively low because of limited cash economies in up-country NWFP. Therefore, subprojects are aimed at minimal investment for collection systems, thereby requiring community support to minimize waste and concentrate waste at neighborhood collection points. Emphasis will be placed on increasing the cash contribution from commercial establishments, especially from wet markets. Collection equipment will be chosen to be affordable, maintainable, and appropriate to the particular urban environment. Disposal management will include equipment and operation systems to compact and cover waste.

E. Roads and Local Access Subprojects

7. Subprojects in the road sector will seek to rehabilitate and improve the main urban road network by resurfacing and widening within the existing right-of-way. Improved access to town centers, and in particular to local neighborhoods, will enhance accessibility for all members of the community as well as increase economic opportunities by attracting investment. Road subprojects include improving associated roadside drains. Part of the subproject will involve traffic management measures to improve circulation in congested town-center areas, through junction improvement and introducing restrictions on parking and roadside vending. Other subprojects will include the extension of the existing road network system to low income areas, where present access is virtually nonexistent.

Table A9: Summary of Subprojects Prepared for Phase 1 Project Towns

Name/Subproject	Present Condition	Rationale	Scope
Charsadda			
Solid Waste Management	<ul style="list-style-type: none"> • Only 12-16 percent of waste collected • Most waste of domestic nature • Inadequate collection and disposal equipment • Uncontrolled dumping 	Subproject should increase the fraction of domestic and commercial waste collected from the urban area, and dispose of it in a more environmentally acceptable manner at improved landfill site	<ul style="list-style-type: none"> • Pilot composting scheme: civil works, equipment • Community self-help collection and disposal: civil works, small equipment • Sanitary landfill sites: development of disposal site and basic operational equipment • Improved collection, transport, and disposal: provision of basic equipment
Swabi			
Road Improvement	<ul style="list-style-type: none"> • Three provincial roads functioning as arterial roads to Swabi town center • Mixture of fast and slow-moving vehicles • All commercial activities along main roads; no parking space; on road loading/unloading • All combined leading to frequent gridlock situation 	<ul style="list-style-type: none"> • Improvement to main urban road networks • Improved traffic management 	<ul style="list-style-type: none"> • Resurfacing, upgrading • Road widening • Improved roadside drains • Improved traffic management
Mansehra			
Water Supply on Gravity Flow	<ul style="list-style-type: none"> • System suffering from high losses • Polluted surface water source • High cost for electricity for deepwell pumps 	<ul style="list-style-type: none"> • Improved quality of supply and quality of water • Increased fraction of pumped and treated water actually delivered and sold to consumer 	<ul style="list-style-type: none"> • Introduction of 5,500 water meters • Leak detection and repair scheme: reduce from 55 percent to 30 percent • Management assistance: prepare operation manual, training, introduction of billing and payment systems, set-up management information system

Name/Subproject	Present Condition	Rationale	Scope
Sanitation			
<ul style="list-style-type: none"> • No piped sewerage system • High incidence of open drains carrying raw sewage 	<ul style="list-style-type: none"> • No piped sewerage system • High incidence of open drains carrying raw sewage 	<ul style="list-style-type: none"> • Sanitation improvements should improve functioning of existing facilities by the providing maintenance equipment; and by improving the flow of the existing network 	<ul style="list-style-type: none"> • (Re)construction of drains (40 hectares) • (Re)construction of septic tanks (18 communal) • Development of sludge drying site with associated infrastructure • Provision of desludging and maintenance equipment (handtools, etc.)
Takht Bhai			
Railway Crossing	<ul style="list-style-type: none"> • Narrow crossing leading to congestion throughout the day • Reduced traffic capacity because of encroachment • Unsafe conditions for pedestrians • Present crossing ill-designed and dangerous • Train three times per week 	<ul style="list-style-type: none"> • A new crossing will improve traffic flow, reduce economic losses caused by congestion, and reduce nuisance for residents and road users 	<ul style="list-style-type: none"> • Relocation of encroaching commercial establishments to be completed before subproject processing • Civil works on railway (removal and clearing ballast), and on roads
Sewerage and Drainage	<ul style="list-style-type: none"> • No piped sewerage system • High incidence of unsanitary methods of disposal of human waste (pit latrine, bucket systems, drain, open space) • PHED to rehabilitate combined drainage network 	<ul style="list-style-type: none"> • Subproject will provide transport and treatment of wastewater. Secondary and tertiary drains will be improved through the PHED-initiated rehabilitation scheme. The subproject will reduce the exposure to contaminated wastewater in the urban area. 	<ul style="list-style-type: none"> • Construction of interceptor sewer • Construction of primary sedimentation ponds • Provision of basic operational and maintenance equipment
Timargara			
Sewerage and Drainage	<ul style="list-style-type: none"> • Drainage systems carry both storm water and sewage • Inadequate drainage capacity in current channels • No interconnected network 	<ul style="list-style-type: none"> • improve flow conditions within drainage network to avoid stagnant polluted water within urban residential area 	<ul style="list-style-type: none"> • Lining of nallas • Improvement of main drainage channels • Construction of interceptor (3,000 m) • Provision of maintenance equipment
Road Improvement	<ul style="list-style-type: none"> • Linear structure of Timargara town, forcing all through traffic to pass through the town • Serious town center congestion 	<ul style="list-style-type: none"> • Improvement to main urban road networks • Improved traffic management 	<ul style="list-style-type: none"> • Resurfacing, upgrading • Road widening, • Improved roadside drains • Improved traffic management

Name/Subproject	Present Condition	Rationale	Scope
Hangu			
Water Supply	<ul style="list-style-type: none"> • <50 percent access to piped water • Low quality of service • Low production capacity • High leakage (50 percent) and wastage • PHED scheme approved (Aug '99) for new sources, reservoir, transmission main, distribution system 	<ul style="list-style-type: none"> • Improved quality of supply and quality of water • Increased fraction of pumped and treated water actually delivered and sold to consumers, should lead to increased revenues 	<ul style="list-style-type: none"> • Leak detection and repair (reduce leakage from 50 percent to 25 percent) • Improvement distribution network (new pipes, sluice valves, air valves, bulk meters) • Management assistance: prepare operation manual; training; introduction of billing and payment systems; setup management information system
Sewerage	<ul style="list-style-type: none"> • No piped sewerage system • Most households PF-systems • High incidence of open drains carrying raw sewage 	<ul style="list-style-type: none"> • Scheme will carry combined storm and wastewater away from residential areas to agricultural land, intended for future treatment • Maintenance should improve flow characteristics of drainage network 	<ul style="list-style-type: none"> • Civil works: construction of combined network for storm and wastewater. Construction of new main drain, rehabilitation of existing open and piped drains. Untreated discharge, possibly used for irrigation as at present • Maintenance equipment

FINANCING ARRANGEMENTS

1. The proceeds of the loan from the Asian Development Bank (ADB) will be onlent by the Government of Pakistan's Ministry of Finance (MOF) to the Department of Finance (DOF) within the Planning and Development Department of the North-West Frontier Province government on the same terms and conditions applicable to ADB's loan to the Government, with a term of 32 years, including a grace period of 8 years, and with an interest rate of 1 percent per annum during the grace period and 1.5 percent per annum thereafter. The Government will assume the foreign exchange risk. In addition, the NWFP Government will provide \$250,000, in foreign currency, to finance the cost of the international municipal financial management advisor position of 13 person-months, as included under the Institutional Development Component.
2. All disbursements for subprojects will be made by the project coordination unit upon endorsement of pertinent project implementation teams and municipal committees (MCs). MCs will be required to borrow an amount equal to a minimum of 20 percent of the subproject cost, and up to 50 percent depending on the MCs financial capacity. The MCs will sign subloan agreements with DOF for the loan portion of the subproject cost, using standard terms and conditions established by DOF, including an interest rate of 7 percent and repayment period of 15 years, and a three-year grace period during which interest payments only will be payable. No interest will accrue on subloans during the construction of subprojects because of the small scale of the loans and the short implementation period. Subject to the demand for loans in the future, DOF may retain principal repayments made by the MCs for relending subject to its obligations to repay funds to MOF to enable MOF to meet the Government's obligations to ADB.
3. The Government will seek the approval of ADB for any significant change to the terms and conditions of the loan agreement between DOF and MOF. A detailed financing plan, by subsector, for both the urban development and institutional development components is shown in Table A10.

Table A10: Detailed Financing Plan by Subsector
(\$ million)

Item	ADB	Domestic			Total
		NWFP Government	Municipal Committees	Subtotal	
A. Urban Development Component					
1. Infrastructure Improvements	16.9	6.5 ^a	0.0	6.5	23.4
2. Community Development and Participation	0.7	0.0	0.0	0.0	0.7
Subtotal (A)	17.6	6.5	0.0	6.5	24.1
B. Institutional Development Component					
1. Implementation Support	1.7	0.0	0.0	0.0	1.7
2. Municipal Finance Capacity Building	1.0	0.2	0.0	0.0	1.2
3. Incremental Administration ^b	0.0	0.7	1.8	2.5	2.5
Subtotal (B)	2.7	0.9	1.8	2.5	5.45
Interest During Construction	0.5	0.0	0.0	0.0	0.5
Total	20.8	7.4	1.8	9.0	30.0
Percentage (%)	69	25	6	30	100

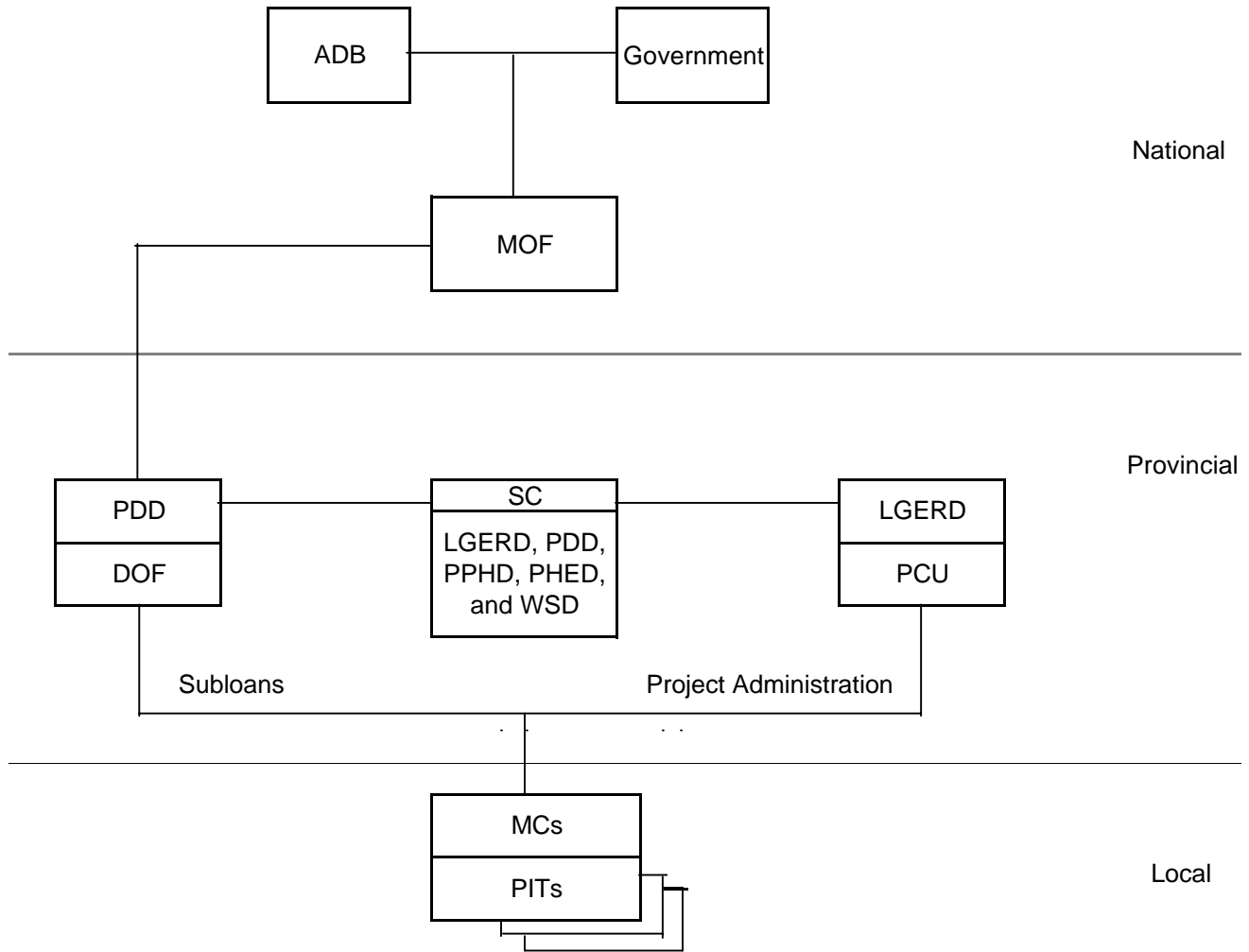
ADB = Asian Development Bank, NWFP = North-West Frontier Province.

^a The Municipal Committees will borrow up to \$4.7 million from project funds through subloans.

^b The project coordinating unit and project implementation teams.

Note: Numbers may not add due to rounding.

PROJECT ORGANIZATION CHART¹



Legend:

- | | |
|--|---|
| ADB = Asian Development Bank | PDD = Planning and Development Department |
| DOF = Department of Finance | PPHD = Physical Planning and Housing Department |
| LGERC = Local Government, Elections and Rural Development Department | PHED = Public Health Engineering Department |
| MC = municipal committee | PCU = project coordination unit |
| MOF = Ministry of Finance | PIT = project implementation team |
| | WSD = Works and Services Department |

¹ Since the NWFP Local Government Ordinance was promulgated in August 2001, the Planning, Environment and Development Department has changed to PDD and PPHD and PHED are expected to reorganized and renamed.

OUTLINE TERMS OF REFERENCE FOR CONSULTING SERVICES

A. Overview

1. Consulting services under the Project are aimed at providing technical, advisory, and managerial assistance in preparing subprojects for implementation, and provide institutional strengthening support to the participating institutions. In total, 36 person-months of international and 360 person-months of domestic consulting are required to carry out the terms of reference associated with the urban infrastructure, community development, and municipal finance components of the Project. Consulting services for the Project are summarized in Table A12.

2. In addition, local North West Frontier Province (NWFP)-based NGOs will be engaged to act as guide and catalyst in the process of establishing sustainable government-community partnerships, for the development of effective and lasting channels of communication.

Table A12.1: Summary of Consulting Services

Position	Input (person-months)		
	International	Domestic	NWFP NGOs
Project Management Support to PCU / PIT	22	192	
Municipal Finance Capacity Building	14	168	
Community Development and Participation			1,320
Total	36	360	1,320

NGO = nongovernment organization, NWFP = North-West Frontier Province, PCU = project coordination unit, PIT = project implementation team.

3. The major tasks associated with the provision of management support during the planning, design and implementation phases of the Project are as follows:

- (i) Assist the project coordination unit (PCU) coordinate the work of the project implementing teams (PITs) and design and supervision consultants.
- (ii) Help the PITs develop annual project work plans, job descriptions, staffing schedules, and equipment budgets.
- (iii) Support the PCU in technical matters such as preparing work orders for the design consultants; reviewing and approving surveys, studies, master plans, subproject final designs, estimates, prequalification of contractors, and contractor's final works; and ensuring sound supervision of subproject construction and any other technical matters arising.
- (iv) Help the PCU and PITs with all aspects of procurement including prequalification of contractors, tender document review, and bid evaluation.
- (v) Assist the PCU with project expansion as a sectoral project, particularly in screening subprojects and also municipal committees (MCs), according to criteria provided, for progressive inclusion into the Project.
- (vi) Assist the PCU and PITs in establishing, testing, and reviewing financial accounting and control systems, and ensuring accurate and timely report submissions and funds flow from the Asian Development Bank (ADB) and to the implementing agencies.
- (vii) Help the participating MCs prepare and review management action plans.
- (viii) In collaboration with the PCU and PITs and implementing agencies, facilitate community participation in subprojects.

- (ix) Ensure that training services contracted to outside organizations are effective and fit within the Project's plans for strengthening MCs.
- (x) With the PCU, ensure the effective and timely delivery of the various institutional development aspects of the Project.
- (xi) Review procedures for construction supervision including quality, cost, and time controls;
- (xii) Help the PCU and PITs monitor and advise the MCs on financial, staffing, and administrative improvements.
- (xiii) Preparing an overall benefit monitoring and evaluation (BME) system for the Project and ensure that the necessary independent inputs are in place when and where required.
- (xiv) Help prepare subproject appraisal reports and obtain ADB approvals.
- (xv) Undertake other tasks as assigned by the Local Government, Elections and Rural Development (LGERD).

4. Additional tasks supporting the community development component include:

- (xvi) Assist the PCU with the design, preparation, planning, and management of the community participation component;
- (xvii) Conduct orientation and inventory of recent and current community-based development initiatives in the North-West Frontier Province (NWFP), organizations involved, mechanisms used, successes achieved;
- (xviii) Help the PCU invite and select nongovernment organizations (NGOs) to be involved in the community participation program; prepare terms of reference (TOR) and job descriptions; interview and brief organizations on project objectives, and discuss proposed role of NGOs;
- (xix) Provide advice on the selection of candidate social organizers (SOs), prepare job descriptions, qualifications required, and search profiles;
- (xx) Plan and deliver initial briefing, training, and orientation of candidate SOs; make data available on program objectives and direction;
- (xxi) Provide continuous guidance on suitable mechanisms for interaction with and training of local government and community-based organizations (CBOs);
- (xxii) Monitor performance of SOs in the field, where necessary make adjustments in program set-up and mechanisms employed; review field reports and advise the PCU on action required;
- (xxiii) Plan and organize regular training events, including workshops and seminars for the duration of the Project;
- (xxiv) Monitor impact of involvement of SOs in project towns; and
- (xxv) Prepare annual reports on performance and impact of community development activities.

5. These services will be provided by an integrated multidisciplinary team of specialists comprising both international and domestic consultants who will report to the project director of the PCU (Table A12.2). The consultants will produce an inception report after one month, progress reports at 3-month intervals, and annual and final reports describing their accomplishments, tasks completed, issues arising, and other supporting documentation.

Table A12.2: Project Management Support to the PCU and PIT

Position	Input (person-months)	
	International	Domestic
Municipal Engineer and Team Leader	22	
Engineers (two)		96
Contract/Procurement Adviser		24
Community Development Adviser		66
BME Adviser		6
Total	22	192

BME = benefit monitoring and evaluation, PCU = project coordination unit, PIT = project implementation team.

6. The principal tasks of the municipal finance capacity building component of the Project include the following:

- (i) Discuss and review the recommendations of previous ADB study (TA 1248-PAK) with provincial and local governments, review the implications of recent and emerging government policies for urban local government finance, and examine the status of municipal finance in the initial group of MCs to participate in the Project.
- (ii) Develop a replicable action program for MCs participating in the Project to (a) introduce a simple computerized double-entry accounting system for municipal finance to replace the current paper-based cash accounting system; (b) provide appropriate reports to facilitate improved financial management, including budgeting, resource mobilization, and enhanced operation and maintenance (O&M) of MC assets; and (c) help MCs meet their financial obligations under the Project, including improving collection of the immovable property tax by the provincial government.
- (iii) Implement the action program for MCs participating in the Project through (a) joint training programs, and (b) locating staff in towns to assist MCs to implement and operate the new accounting system, to generate and use management information reports, and to initiate programs to assist MCs to meet their financial obligations under the Project.
- (iv) Provide continuing advice and support to MCs as needed.
- (v) Disseminate information on improved municipal financial management to all MCs and town committees (TCs) in NWFP through seminars, materials, and training.
- (vi) Help develop a management information system for MCs.

7. The consultants will be based in the PCU, and will maintain close links with the Local Council Board. Much of the work will be undertaken by consultants located in the MCs, where they can assist MCs to implement new practices. Estimated consultant resources needed to undertake the tasks are described in Table A12.3.

Table 3: Municipal Finance Capacity Building

Position	Input (person-months)	
	International	Domestic
Municipal Finance Management Adviser	14	
Financial Management /Institutional Development Expert		24
Management Information System Expert		18
Programmers (3x12 months)		36
Training Adviser		12
Accountant (3 months per town)		78
Total	14	168

8. The consultants will prepare (i) an inception report within six weeks of commencing work to report on the initial review of municipal finance and a program of subsequent activities; (ii) a report describing the proposed municipal finance action plan to be implemented in project MCs, to be provided prior to implementation of the action plan; (iii) a progress report following implementation of the action plan in the first phase MCs, including recommendations for improvements to action plans for subsequent MCs; (iv) a report containing training material and reports of training programs undertaken; and (v) progress reports following implementation of the action plan for MCs in the second and third phases of the Project.

9. The services will be provided through one or more NGOs originating from and based in NWFP, contracted directly by LGERD. NGOs committed to the development of (urban) CBOs, (urban) local government, and issues of devolution and decentralization will be recruited in accordance with Planning Environment and Development Department (PEDD) guidelines on the recruitment of NGOs, by a committee comprising members from Finance, PEDD, LGERD, and the (PMU), through direct invitation or following public notification. The NGOs will enter into an agreement with the Government on the form and content of the provision of the services of teams of SOs, to be based in each project town.

10. A team of SOs will consist of one female and one male SO. The team will work in the project town for the duration of the project, from the point of confirmed selection of the town, until completion of the implementation of subproject components, expected to be three years. Preferably, the team will be recruited from the relevant district (i) to ensure cultural affinity and language compatibility with the communities, and (ii) to avoid logistical problems of transport and accommodation. SOs are likely to operate from the offices of the MC.

11. Upon appointment by the PCU, the NGOs will select teams of SOs for the phase 1 project towns. The NGO will be responsible for the selection process, according to outline job descriptions and qualification requirements as specified by the PCU. Before the start of their involvement, candidate SOs will be trained at the provincial level under guidance of the senior community development adviser (CDA), who has overall responsibility for the planning and implementation of the community development process. The training will focus on clarifying the role of the SOs in the process, nature, and objectives of the overall Project; some fundamentals on urban services and infrastructure; and the functioning and organization of (urban) local government and the municipal committee in particular. Experience can be drawn from other successful community-based projects in NWFP on appropriate forms of organizing and training large groups of SOs.

12. During the course of the Project, senior SOs will be selected based on experience and organizational aptitude to take on a wider role in administration, training, and dissemination of collective experience. During the course of the Project, some organizational structure will evolve within the group of SOs, with more experienced SOs assuming a regional management role, and liaison for practical purposes between town teams and the central PCU.

13. Tasks for the SOs include the following:

- (i) Receive training and orientation at the PCU on the project framework and the overall developmental objectives;
- (ii) Became familiar with available relevant socioeconomic data from earlier studies and surveys on project town: social profile, priorities on service provision, records on fee payments (data to be provided by the PCU);
- (iii) Map population groups in project town assigned; inventory social groups and existing CBOs; report on functioning of existing CBOs, record nature, purpose, composition, and method of operation;
- (iv) Gain insight on the operation of the MC; plan, organize, and conduct exploratory meetings with key municipal staff, explaining objectives of involvement in the development program;
- (v) Maintain close coordination with the PIT, in particular with the community liaison officer (CLO) within the team, and keep informed on planning process; train the CLO, jointly define role and method of operation;
- (vi) Through interviews and from observation, assess the level, purpose, and mechanism of current interaction between MC and the population, whether as individuals, representative organizations, or lobby groups;
- (vii) Plan, prepare, and conduct a series of joint meetings or workshops between CBOs (representatives) and MC staff, to discuss mutual expectations and priorities on respective roles in town management, and on means to improve constructive communication and collaboration; discuss and identify potential roles of communities in planning and delivering urban services and infrastructure; achieve joint understanding on common objectives; explore and identify common benefits;
- (viii) Plan, prepare, and conduct meetings, workshops, and training seminars for MC staff at all levels, to discuss actual and assigned role and responsibilities of local government in service delivery and improve performance;
- (ix) Plan, organize, and deliver public awareness campaigns for specific subprojects; improve awareness among communities on impact of their living environment and family health; explain reason for and benefit of certain sanitation improvements and need for charges to maintain certain services; and
- (x) Act as liaison and catalyst between communities and other sources of support in other sectors, such as health, education, and employment generation; and provide guidance on how to access other support programs.

14. Estimates for the input of SOs (Table A12.4) are based on (i) a team of one female and one male SO per project town; (ii) for the entire period of the project, including initial planning, subproject selection and appraisal, bid preparation and evaluation, and implementation of subprojects, estimated as approximately three year; and (iii) for a total of 17 project towns. Actual inputs per town are bound to vary, as may be total number of participating towns.

15. Additional input is identified for senior management time of the NGO(s) involved, reflecting planning, organization, and management at the provincial level between the NGO and the PCU. Financial provision has been made for training and support material.

Table A12.4: Community Development and Participation

Position	Domestic NWFP NGOs
Male Social Organizers, one per town for three years	620
Female Social Organizers, one per town for three years	620
NGO coordination and management	80
Total	1,320

NGO = nongovernment organization, NWFP = North-West Frontier Province.

16. The team will prepare a brief monthly report to the CDA, according to a format and style specified during initial training. The purpose of the reports is to (i) record the nature, purpose, composition, and operational methods of existing CBOs, and of new ones as they develop; (ii) record progress with the process of capacity building within the MC; and (iii) document achievements mobilizing communities.

IMPLEMENTATION SCHEDULE

		Year 1				Year 2				Year 3				Year 4				Year 5				Year 6			
		1	2	3	4	1	2	3	4	1	2	3	4	1	2	3	4	1	2	3	4	1	2	3	4
	Loan Effectiveness																								
	Establishment of PCU and PITs																								
Urban Infrastructure																									
Phase 1 towns																									
	Detailed design, prepare tender docs																								
	Bid evaluation, award contracts																								
	Construction, implement subprojects																								
Phase 2 towns																									
	Selection of phase 2 towns																								
	Subproject selection, appraisal																								
	Detailed design, prepare tender docs																								
	Bid evaluation, award contracts																								
	Construction, implement subprojects																								
Phase 3 towns																									
	Selection of phase 3 towns																								
	Subproject selection, appraisal																								
	Detailed design, prepare tender docs																								
	Bid evaluation, award contracts																								
	Construction, implement subprojects																								
Institutional Strengthening																									
	Technical assistance, project management																								
	Municipal finance capacity building																								
	Community development and participation																								
	Midterm review																								
	Benefit monitoring and evaluation																								

ECONOMIC AND FINANCIAL ANALYSES OF TYPICAL SUBPROJECTS

1. The broad range of economic benefits that are expected to result from subprojects is outlined in Table A14.1. Economic internal rates of return (EIRRs) and financial internal rates of return (FIRRs), as appropriate, were prepared for representative subprojects in accordance with the Asian Development Bank's (ADB) *Framework for the Economic and Financial Appraisal of Urban Development Sector Projects*. EIRRs were prepared for road and drainage subprojects (Table A14.2), and FIRRs for solid waste disposal and water supply subprojects (Table A14.3).

2. Financial evaluations were based on current fees paid by consumers and indications of willingness to pay for improved services, determined on the basis of a socioeconomic survey of households. However, the surveys generally indicated a low willingness to pay, apparently reflecting doubts by potential beneficiaries about the capacity of government to deliver effective projects and an underestimation of the impact of projects on their lives. Economic evaluations were based on the domestic price numeraire, and exclude taxes (at a rate of 10 percent) and other market distortions (with a standard conversion factor of 0.85). A shadow exchange rate factor was applied to tradable components of the project costs. Projects were assessed over a 20-year evaluation period, with allowance made for the residual value of assets at the end of the evaluation period. The evaluations were undertaken using constant 1999 prices, and took into account incremental operation and maintenance (O&M) costs. The minimum acceptable EIRR should be 12 percent, and FIRRs for subprojects should exceed the real weighted average cost of capital, which is estimated at 2.5 percent. However, the community development and participation component of the Project is designed to increase public understanding and ownership of subprojects, and thus improve beneficiary perception of the effective delivery of services and understanding of the benefits that will result. The higher willingness to pay that should result will increase the value of the subprojects, which are conservatively based on current willingness to pay.

A. Drainage and Sanitation

3. Storm-water drainage subprojects involve rehabilitating and upgrading existing drains, and some development of new drains, to establish an interconnected network with suitable outflow arrangements. The subprojects will reduce the incidence of inundation, which is severe in some towns with flat terrain, and reduce the incidence of erosion in towns where the terrain leads to rapid runoff of storm water. The former will result in reduced damage to property, improved quality of life, and health benefits. These benefits will be reflected, to some extent, in increased property values following implementation of the subprojects. Drainage subprojects will reduce property damage, social dislocation and health impacts, and economic dislocation. The value of such benefits will often be difficult to explicitly identify and value, but willingness by beneficiaries to pay for the benefits will normally provide an indication of their value. It is probable that some of the social benefits from reduced flooding and environmental benefits from reduced erosion may not be fully reflected through indications of willingness to pay. This may warrant acceptance of subprojects that have lower EIRRs but where unquantifiable social and environmental benefits are expected to be major benefits. No pure drainage subprojects have been prepared for the initial project towns, and hence no evaluation has been undertaken.

4. Sanitation improvements will generally involve the provision of individual and communal septic tanks, which, in conjunction with drainage subprojects, will result in diversion of outflows from septic tanks and household wastewater away from residential areas and for outflow to occur in suitable locations. The improved sanitary conditions that will result will provide health

benefits and savings in medical expenditure. Socioeconomic surveys for the project towns indicate only limited current willingness by the community to pay for improved services, at about PRs11 per household per month for improved drainage and sanitation. This occurs despite current high levels of morbidity due to waterborne diseases, with 63 percent of households in the initial project towns reporting illness in the household in the month before the survey. The principal illnesses were malaria (26 percent), diarrhea (23 percent), and typhoid (14 percent), all of which are related to poor water management.

5. A financial evaluation was prepared for the component of a subproject in Takht Bai, which would provide treatment of wastewater and removal via improved secondary and tertiary drains, which will reduce exposure of residents in the urban area to contaminated wastewater. Based on the currently expressed willingness to pay, the FIRR for the subproject is estimated at 6.1 percent (Table A14.2). This FIRR would increase substantially if community perceptions of the merits of the subproject were improved and the willingness to pay increased accordingly.

B. Solid Waste Disposal

6. Solid waste subprojects involve development of new disposal sites, procurement of units for the collection of solid waste, and improved treatment of solid waste. The subprojects have environmental and health benefits that warrant acceptance of a hurdle rate that is less than the opportunity cost of capital associated with the Project. Socioeconomic surveys for the project towns indicate a negligible current willingness by the community to pay for improved services.

7. A financial evaluation was prepared for a subproject to develop an improved system of self-help collection and disposal of solid waste in Charsadda through community mobilization, the purchase of relevant collection and disposal equipment, and development of a waste disposal site. Socioeconomic surveys for the project towns indicate a low current willingness by the community to pay for improved urban services, but the community development and participation component of the Project are expected to improve beneficiary perception of the effective delivery of waste collection services and understanding of the benefits that will result. The combination of a current willingness to pay of PRs11 per household per month and a reduction in the cost of maintaining drains because of the reduced quantity of waste disposed of in drains results in an FIRR for the subproject of 7.1 percent (Table A14.3). This FIRR would increase substantially if community perceptions of the merits of the subproject were improved and the willingness to pay increased accordingly.

C. Water Supply

8. Water supply subprojects will generally involve rehabilitation of and extensions to existing systems to improve the quantity and quality of water supply, and reduced technical and administrative losses. Reductions in physical losses of water and wasted water will allow additional water to be supplied to new consumers without the need to increase the supply of raw water. A financial evaluation was prepared for a water supply subproject in Hangu to reduce physical water leakage, improve the water distribution system, and introduce water meters. The benefits of the subproject will be to release current water that can be sold to new customers. Based on projected water tariffs (PRs85 per household per month, which is equal to 2 percent of average 25th percentile household income of PRs4,500 per household per month, with a 5 percent per annum real increase in the water tariff), the FIRR for the subproject is estimated to be 10.6 percent (Table A14.3).

D. Roads

9. Road improvements will include improvements to the surface and alignment of existing roads, widening of existing roads, and to a lesser extent, construction of new streets. Benefits include savings in vehicle operating costs (VOCs) and personal travel time (business purposes), and increased accessibility for development. The last of these benefits is reflected in higher land values, but is excluded because of the risk of double-counting the benefits, and the difficulty of accurately depicting increases in land value that can be attributed to improved accessibility. Savings in VOCs resulting from road improvements take into account the effect of higher travel speed and reduced road roughness on VOCs as derived by the Ministry of Communications. Savings in personal travel time were based on trips for work purposes only. Incremental O&M costs were estimated at 0.4 percent of the capital cost of subprojects, plus an allowance of 20 percent of the capital cost every seven years for resurfacing. The economic life of road improvement subprojects is 20 years.

10. An economic evaluation was prepared for the subproject to improve an at-grade railway crossing in Takht Bai to improve traffic movement and reduce delays. The crossing is heavily used, and the improvement results in an EIRR of 17 percent (Table A14.2). Savings in VOCs account for 40 percent of the benefits; and savings in personal travel time account for the remaining benefits. Overall, the road subprojects in the central areas of towns are expected to have high EIRRs because of the concentration of traffic in those areas and the poor quality of existing roads. Rehabilitation of existing roads will also generally have higher EIRRs because of the considerable savings in travel time and, in particular VOCs, which can result from relatively modest expenditure. New roads to developing areas at the periphery of towns are likely to have lower EIRRs, but may be warranted in some circumstances.

Table A14.1: Summary of Economic Benefits of Subprojects

Benefit	Solid Waste	Water Supply	Roads	Drainage	Sanitation
Health & Environment					
Reduced waterborne diseases	High	High		High	Medium
Reduced fly/mosquito breeding	High	High		High	High
Decreased infant mortality	Medium			Medium	Medium
Less sick time off from work	Medium	Medium		Medium	Medium
Improved school attendance	Medium	Medium		Medium	Medium
Savings in medical costs	Medium	Medium	Medium	Medium	Medium
Improved hygiene standards	High	High		High	High
Pollution abatement	High	High	Medium	High	High
Fewer road accidents			High		
Infrastructure and Financial					
Expanded land use and availability	Low		Medium	High	
Increased land/property values	Low	High	High	High	
Increased MC revenue	Medium	High	Medium	Medium	
Reduced MC O&M costs	High	Medium	Low	Medium	
Reduced damage to crops/livestock	Low			High	
Reduced road maintenance costs			High	High	
Reduced vehicle operating costs			High	Medium	

Benefit	Solid Waste	Water Supply	Roads	Drainage	Sanitation
Reduced travel time			High	High	
Improved accessibility of markets			High	Medium	
Socioeconomic Development					
Improved municipal service levels	High	High	High	High	
Improved trade and business	High	High	High	High	High
Employment impacts	Medium		High	Medium	
Reduced household maintenance	High	Medium	Low	Medium	Medium
Improved living standards	High	High	High	High	High
Greater productivity of MC staff	High	High	High	High	

MC = municipal committees, O&M = operation and maintenance.

Table A14.2: Summary of Economic Evaluations

Component/Location	Economic Internal Rate of Return (%)					
	Base Case	Case 1 (Capital Cost +10%)	Case 2 (Benefit -10%)	Case 3 (Delayed Benefits 1 year)	Case 4 (1+2)	Case 5 (1+2+3)
Road Improvement, Takht Bai	17.3	15.7	15.3	14.2	13.9	12.6
Sanitation and Drainage Rehabilitation, Takht Bai	6.1	5.4	5.2	4.6	4.6	4.1

Table A14.3: Summary of Financial Evaluations

Component/Location	Financial Internal Rate of Return (%)					
	Base Case	Case 1 (Capital Cost +10%)	Case 2 (Benefit -10%)	Case 3 (Delayed Benefits 1 year)	Case 4 (1+2)	Case 5 (1+2+3)
Solid Waste Improvement, Charsadda	7.1	6.0	5.6	5.4	4.6	4.1
Water Supply, Hangu	10.6	9.5	9.2	8.7	8.2	7.5

SOCIAL ASPECTS AND AFFORDABILITY

A. Introduction

1. Social development concerns, including gender, poverty, and community participation, have been incorporated into all stages of project preparation. Gender, poverty, and public welfare issues were the bases of approaches used in socioeconomic and urban data collection during the project preparatory technical assistance, particularly in the design of the household perception survey and the survey of current services and social and physical infrastructure in the initial project towns, and in the sector and subsector assessments. Social and economic issues influenced the selection and design of the urban infrastructure, community development, and participation components of the Project. The involvement of the public in subprojects will complement and reinforce the immediate economic and health benefits associated with water supply, drainage, sanitation, and solid waste management components of the Project by ensuring sustainability and ownership.

B. Socioeconomic Profile of Urban Households

2. The average household size in the initial project towns is 7.7, with an average of 1.2 families per household.

3. Average household monthly income is estimated to be PRs9,800, with the 25th percentile and medium income at PRs4,400 and PRs7,100 respectively (Table A15.1), indicating a substantial unequal distribution of income in the community. About two thirds of income for both average and 25th percentile income households is spent on food, clothing, rent, electricity, fuel, and water, with only 0.4 percent of income for both categories of household spent on water. The amount spent on water is only 4 percent of that spent on electricity and fuel.

4. Household ownership is high, at 86 percent of households, with an average of one fifth of houses being katcha (permanent mud-formed structures). Flooding is a problem for many, with 17 percent of households reporting that floodwater enters their homes. The supply of services to households includes a low 26 percent for solid waste collection, 37 percent have piped water supply, and 40 percent have a septic tank. The current moderate residential density away from town centers alleviates the difficulties of these service levels. However, high average population growth of 3.6 percent per annum will increase the need for higher levels of service in the future.

C. Gender

5. The ratio of women in urban households in the initial project towns is low in comparison with demographic norms, with an average of only 93 women for every 100 men in urban households. Women also remain almost exclusively tied to household activities, wives make up only 3 percent of employed household members, compared with husbands at 86 percent, children at 8 percent, and other household members, 3 percent.

6. Women in Pakistan bear primary responsibility for management of the domestic environment, including water collection and solid waste disposal. Children also participate significantly in these activities. Women will therefore benefit directly from

project activities that improve sanitary conditions in the immediate surrounding area of homes (improved removal of wastewater and solid waste collection). Women will also benefit from drainage projects that reduce the incidence of flooding of houses and the damage and dislocation that results.

D. Affordability to Beneficiaries

7. A review of the components and subcomponents included in the Project reveals that the direct and indirect repayment burdens imposed on beneficiaries are generally affordable to all benefiting social and income groups. The affordability implications for particular subcomponents are discussed in the following subsections.

1. Immovable Property Tax

8. Current collection of the immovable property tax varies considerably between the initial project towns, ranging from PRs0 to PRs41 per capita per annum, equal to a maximum of 0.03 percent of average household income and 0.08 percent of first quartile income households, and generally a markedly lower share for most urban residents. Substantial increases in revenue from the immovable property tax are expected only in towns where rates are low at present. Hence, the need to increase resource mobilization through the immovable property tax should not generally present a burden to communities. The immovable property tax is mildly progressive because very small allotments (of less than approximately 38 square meters) pay no tax, although this effect is diminished by a relatively higher rate of tax for small to medium-size allotments (5-10 marla) than for larger properties. The Tax could be made more progressive by ensuring that the unit tax rate rises with property size.

2. Water, Drainage, Sanitation, and Solid Waste Charges

9. Surveys indicate only limited current willingness by the community to pay for improved services (e.g., about PRs11 per household per month for improved drainage and sanitation services, and PRs26 per household per month for improved water supply). This occurs despite current high levels of morbidity due to waterborne diseases, with 63 percent of households in the initial project towns reporting illness in the household in the month before the survey. The principal illnesses were malaria (26 percent), diarrhea (23 percent), and typhoid (14 percent). Proposed subprojects will contribute to a reduction in these water-related illnesses by improving the removal of wastewater and solid waste, and reducing the unnecessary presence of still water. The community development and participation component of the Project is designed to increase public understanding and ownership of subprojects, and thus improve beneficiary perception of the effective delivery of services and understanding of the benefits that will result.

10. A proposed increase in the cost of water, on an incremental basis over the first two years of the project implementation, of PRs85 per household per month, will result in a tariff that is equal to 2 percent of average 25th percentile household income of PRs4,400 per household per month, which indicates that continuing real increases in water tariffs (which will be offset to some extent by rising household income) can occur, while still ensuring adequate access by low income households to water. Similarly, charges for removal of solid waste and for drainage and sanitation improvements should be affordable to beneficiary communities.