



Indonesia Infrastructure  
Initiative

**Project Design Document**

**Australia Indonesia Infrastructure Grants  
for Municipal Sanitation**

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## **Abstract**

*This Program Design Document describes the Australia Indonesia Infrastructure grants for municipal sanitation (sAIIG) to be implemented over three years from 2012 to 2014. The sAIIG is designed to stimulate local government investment in municipal infrastructure for sanitation, and to provide incentives for governance reforms that will impact sanitation and other sectors.*

*The Government of Indonesia will award sAIIG to select LGs using the GoI on-granting regulations. Funds will be disbursed using an output-based modality after the LG has implemented the sanitation infrastructure stipulated in the grant agreement, and after the works have been verified as acceptable. The GoI will select LGs through an assessment of the governance credentials of the LGs, and evidence of their capacity to implement sanitation programs. To retain the grants throughout the program life, LGs will have to demonstrate progressive attainment of governance benchmarks.*

*The sAIIG concept is an extension of the Infrastructure Enhancement Grants (IEG) for municipal sanitation, which was implemented as a pilot program during Phase I of IndII. The sAIIG incorporates important lessons learned during that earlier activity, most significant of which was to adopt an output-based modality, and reduce the types of infrastructure eligible for grants. Neighbourhood sewerage with treatment, or with a connection to existing sewerage, and solid waste transfer stations comprise the eligible grant components of the sAIIG.*



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## Acronyms and Abbreviations

AIIG	Australia Indonesia Infrastructure Grants
AIP-CS	Australia-Indonesia Partnership (AIP 2008-13)
AMDAL	Environmental Impact Assessment <i>Analisa Mengenai Dampak Lingkungan</i>
APBD	LG budget of income & expenditure <i>Anggaran Pendapatan dan Belanja Daerah</i>
APBN	Gol budget of income & expenditure <i>Anggaran Pendapatan dan Belanja Negara</i>
BAPPENAS	National Development Planning Agency
BI	Bank Indonesia
BLUD	Local Public Service Delivery Agency <i>Badan Layanan Umum Daerah</i>
BPK	State Audit Board <i>Badan Pemeriksaa Keuangan</i>
BPKP	Finance and Development Supervisory Board <i>Badan Pengawasan Keuangan Dan Pembangunan</i>
CLTS	Community-Led Total Sanitation
CSS	City Sanitation Strategy
DAK	Special Allocation Grant (to LG) <i>Dana Alokasi Khusus</i>
DEWATS	Decentralised wastewater treatment system
Dir. PLP	Directorate of Environmental Sanitation at DGHS <i>Penyehatan Lingkungan Permukiman</i>
DGHS	Directorate General of Human Settlements, Ministry of Public Works
DJPB	Directorate General of Treasury, Ministry of Public Works
DGFB	Directorate General of Fiscal Balance, Ministry of Finance
DPRD	Local Community Council <i>Dewan Perwakilan Rakyat Daerah</i>
EIA	Environmental Impact Assessment
GoA	Government of Australia
Gol	Government of Indonesia
IEG	Infrastructure Enhancement Grant
JMP	WHO / UNICEF Joint Monitoring Programme
KPK	Corruption Eradication Commission <i>Komisi Pemberantasan Korupsi</i>
LG	Local Government - City or Regency (Kota or Kabupaten)
LGDP	Local Government and Dentralsation Project (of the World Bank)
MCK	municipal communal toilet and ablution blocks
MDB	Multilateral Development Banks
MoF	Ministry of Finance
MoH	Ministry of Health
MoHA	Ministry of Home Affairs
MPSS	Program Memorandum for the Sanitation Sector
MPW	Ministry of Public Works
MSMHP	Metropolitan Sanitation Management and Health Programme
PAL	Wastewater Management <i>Pengelolaan Air Limbah</i>
PAMSIMAS	Community-based Water Supply and Sanitation <i>Penyediaan Air Minum dan Sanitasi Berbasis Masyarakat</i>
PDD	Program Design Document (this document)
PIU	Project Implementation Unit
PNPM Mandiri	National Program for Reducing Poverty through Community Empowerment <i>Pengendali Penanggulangan Kemiskinan Berbasis Pemberdayaan Masyarakat</i>
PPH	On-granting Agreement between DGHS and LG

PPSP	Accelerated programme of urban sanitation development <i>Percepatkan Pembangunan Sanitasi Permukiman</i>
RKL	Environmental Management Plan
RKM	Community Work Plan <i>Rencana Kerja Masyarakat</i>
RPL	Environmental Monitoring Plan
RPIJM	Planned Medium Term Investment Programme <i>Rencana Program Investasi Jangka Menengah</i>
RPJMN	National Medium Term Development Plan 2010 - 2014
sAIIG	Australia Indonesia Infrastructure Grants - Sanitation
SANIMAS	Community-based Sanitation <i>Sanitasi Oleh Masyarakat</i>
SEA	Strategic Impact Assessment
SKPD	Local Task Force under PIU <i>Satuan Kerja Perangkat Daerah</i>
WASAP	Water and Sanitation Program Trust Fund - World Bank administered
WASPOLA	Water and Sanitation Policy Assistance Project
WB	World Bank
WSP	Water and Sanitation Program - World Bank partnership with Gol
UPTD	Technical Service Unit <i>Unit Pelaksana Teknis Daerah</i>



# 1 EXECUTIVE SUMMARY

## 1.1 Background

Sanitation in Indonesia lags significantly behind its ASEAN neighbours. UNDP data shows improved sanitation facilities cover 67% of the urban population while some 9% use shared facilities, 8% use unimproved facilities, and an estimated 16% practice open defecation. Municipal services for solid waste sector are equally poor. Less than 50% of the household waste is disposed of in landfills, and very few landfills are operated in accordance with good sanitary disposal practice. Efforts to increase basic sanitation coverage are being set back by population growth, as investments in facilities have failed to keep pace with the growth in urban populations

Decentralisation has devolved considerable authority and responsibility in the sanitation sector to the LGs. During the past decade however, the engagement of LGs in the sector has been minimal. Current funding arrangements such as transfers, loans and subsidies deliver sanitation investments through national channels, or bypass LGs in favour of community initiatives. The sAIG program is designed to re-engage LGs in the sanitation sector by providing incentives for investment and also to develop the grant channel as a new vehicle for transferring national subsidies for LGs.

## 1.2 The sAIG

The sanitation AIG will provide \$40 million in grants over a three-year period to approximately 40 selected local governments for implementing municipal sanitation infrastructure using an output-based modality. The sAIG will provide improved sanitation to approximately 92,000 households or 400,000 beneficiaries. The terms of each grant will be defined in an on-granting agreement and the LGs will implement the program using Gol systems and procedures. The local governments will pre-finance the implementation and will claim reimbursement after verification of the completed works. The DGHS will ensure that LGs comply with the provisions of a Project Management Manual issued by decree of the Director General of Human Settlements and referenced in the on-granting agreements.

### 1.2.1 Components

***Neighbourhood sewerage plus treatment*** - These will be simplified sewerage systems, designed for gravity flow only, of shallow depths (less than 1.5 metres), with no manholes or pumping stations but with inspection chambers and cleanouts. Typically each system will serve between 50 and 400 households. Treatment will consist of an appropriate anaerobic process but will not be prescribed. Effluent quality must meet Gol Ministry of Environment requirements.

***Neighbourhood sewerage connected to existing sewerage system*** - These will be identical to the neighbourhood schemes above except that in cities with existing sewerage schemes, the neighbourhood schemes may connect to the live sewer so that treatment will be provided by the existing facilities.

***Intermediate Solid Waste Transfer Stations*** - Intermediate Transfer Stations (*Stasiun Peralihan Antara*, or SPA) receive solid waste from various sources, aggregate and compact it for haulage to the final disposal site. These facilities may vary in size from 5,000 m<sup>2</sup> to more than 10,000 m<sup>2</sup>.

### **1.2.2 Goal and Objectives**

The goal of the sAIG is to increase the provision of improved sanitation facilities by Local Government through the implementation of public sanitation infrastructure.

The project development objectives are to:

- (a) Increase LG investment in sanitation infrastructure that will contribute to meeting the GoI and MDG sanitation service targets by providing up to \$40 million in output-based grants to 40 LGs that are willing to pre-finance \$60 million of sanitation infrastructure during the three-year period 2012–2014.
- (b) Improve governance in the sanitation sector at these LGs by requiring them to adhere to an agreed multi-year sanitation investment program and to make specific incremental improvements in governance.

### **1.3 Level of the grant**

The grant for neighbourhood sewerage plus treatment will be set at IDR 4,000,000 for each verified connection to a household.

The grant for neighbourhood sewerage connecting to existing mains sewers will be set IDR 3,000,000 for each verified connection to a household.

The sAIG does not pre-assign a unit cost for intermediate solid waste treatment facilities; rather each proposal will be reviewed, and a cost for the facility determined. The grant will be fixed at 50% of the agreed cost. The grant will then be paid on satisfactory completion of the works.

### **1.4 Implementation arrangements**

The program will be implemented through GoI systems and procedures. A direct funding agreement will be signed by GoI and AusAID, and GoI will establish a special account in Bank Indonesia, to which the grant funds will be transferred. The executing agency for the program will be DGHS. A central project management unit and Project Management Manual will be established by decree of the Director General of Human Settlements. DGHS will bear principal responsibility for selecting the participating LGs, using entry criteria agreed in the project design. Entry criteria include evidence of commitments to achieve governance benchmarks that will be stated in the grant agreements. Proposals for the award of grants will be sent from DGHS (in consultation with AusAID) to MoF, which will issue a notification of the grant award. MoF will subsequently sign a three-year grant agreement with each LG. The grant agreements will include reference to the DGHS project management manual which will contain detailed implementation guidelines. Day-to-day management of the program will be the responsibility of a DGHS project management unit which will be supported by consultants engaged by IndII.

### **1.5 Partner Agency commitment**

The partner agency, DGHS, endorses the output-based design of the sAIG. Both DGHS and the Directorate General of Fiscal Balance (DGFB) have participated in the design of the sAIG for IndII Phase II. DGHS has established a team to support IndII during the design progress. DGHS has also committed budget funds equivalent to \$0.6 million for a Central Project Management Unit (CPMU) to oversee the implementation of the sAIG activity.

## **1.6 Verification**

Verification will occur at two points: first, during the qualification process, and second on inspection of completed outputs. Before funds are committed, the CPMU, assisted by IndII, must approve the LG's proposed program. The approval will determine whether the LG's plans meet standards described in the PMM regarding land acquisition, social and environmental safeguards, design, and procurement documents. When the infrastructure is completed, the LG will request a verification review by the CPMU. IndII proposes to examine the possibility of progressive engagement with BPKP to participate in the second-stage verification process, giving Gol greater ownership of the process and mainstreaming the procedure.

## **1.7 Cross cutting issues**

The program includes comprehensive attention to cross cutting issues in conformance with both Gol and AusAID guidelines covering poverty, disability, gender equality, child protection, and environmental compliance. IndII consultants will support LGs to disseminate poverty, disability and gender issues among relevant LG departments involved in the implementation of the sAIG.

## **1.8 Technical assistance**

The sAIG design recognises that implementing a sewerage program for households is more complex than providing water connections through the Water Hibah. Therefore, in addition to the usual baseline, verification and oversight consultants, greater resources are being allocated to: build LG capacity; support LGs as they review and improve designs; and assess readiness in terms of land acquisition and environmental compliance. These consultants will be engaged by IndII and will work with the DGHS implementing units.

## **1.9 Critical risks and risk management strategies**

The use of the output-based modality will significantly reduce grant implementation risks. Adequate safeguards are in place to detect the misuse of grant funds and to intervene as required. This intervention increases the possibility that allocated funds will not be disbursed. Many of the identified risks are related to procurement and implementation. The use of an output-based mechanism for administering the grant will reduce the procurement risks but not eliminate them. Construction quality will also remain an issue. For those reasons, procurement quality will be one of the key governance benchmarks in the grant agreements and a central requirement for LGs in retaining the grant awards. Construction quality will be addressed through dedicated field supervision and periodic review, prior to the handover of completed works, by independent consultants engaged under IndII contract. Post-procurement audits will be carried out periodically by the independent review consultant.

Additional monitoring and oversight will be achieved through a publicly accessible web site promulgating the program and the award of grants to LGs. Such websites have served as effective tools for good governance in PNPM, Pamsimas, and other projects. LGs will be required to establish sAIG-specific websites or promote sAIG content in their own websites to disseminate, at a minimum, the status of implementation, tenders, and results of procurement.

## 2 ANALYSIS AND STRATEGIC CONTEXT

### 2.1 Country and sector issues

Sanitation service coverage in Indonesia lags significantly behind its ASEAN neighbours. A recent UN report notes that improved sanitation facilities cover 67% of the urban population while some 9% use shared facilities, 8% use unimproved facilities, and an estimated 16% practice open defecation.<sup>1</sup> Municipal services for solid waste sector are equally poor. Less than 50% of the household waste is disposed of in landfills, and very few landfills are operated in accordance with good sanitary disposal practice.

*Present status lagging ASEAN countries.*

Efforts to increase basic sanitation coverage are being set back by population growth. Investments in sanitation facilities have failed to keep pace with the growth in urban populations while the use of household on-site sanitation systems has not been accompanied by commensurate public investments in infrastructure for collection, treatment and disposal of waste.<sup>2</sup>

*Not keeping pace with urbanisation. Lack of public investment by LGs.*

Whilst the delivery of sanitation services has been largely decentralised to LGs, funding arrangements remain highly centralised. Recent reviews of expenditure<sup>3</sup> of central and local governments show that LGs' overall expenditure for infrastructure is approximately equal to that of the central government. However, in terms of proportions devoted to sanitation investments, central agencies on average spend 7-8 times more than LGs.<sup>4</sup> For example, the MPW-approved sanitation budget for 2011 is \$300 million. This greatly exceeds the Gol DAK<sup>5</sup> to LG for sanitation, which in 2011 was just \$45 million shared amongst 428 LGs (with an average allocation of slightly more than \$100,000).

*Gol funding is still skewed towards central ministries. Lack of funding for LG sanitation programs.*

Despite decentralisation of responsibilities, LGs are not fully aware of the important health and economic benefits of sanitation and this is reflected in lower budget allocations. Constituents have a long-established tolerance for poor sanitary conditions, a poor understanding of sanitation benefits and do not actively pressure their local governments for improvements. Local governments have historically viewed sanitation as a private responsibility and have limited their investments to servicing private sanitation infrastructure.<sup>6</sup>

*Sanitation is a low priority for LG. LGs lack capacity.*

The Gol has initiated a policy to address the deficiency of sanitation services as part of a broader policy platform that responds to related issues of poverty and health in both urban and rural settings. The most significant thrust of the policy is a doubling of the sanitation sector budget in the 2010–2014 RPJM compared to the previous RPJM budget - to \$1.7 billion. The Gol has also emphasised the importance of sanitation by creating a separate sanitation category in the DAK starting in 2010.

*Gol policy to redress slow progress with sanitation sector.*

At the operational level, sectoral ministries under the leadership of Bappenas have initiated the PPSP program as one part of the national policy to accelerate sanitation

*PPSP Coordinated Ministry initiative for*

<sup>1</sup> WHO / UNICEF Joint Monitoring Programme for Water Supply and Sanitation Estimates for the Use of Improved Sanitation Facilities. Updated March 2010. Indonesia.

<sup>2</sup> National population growth 1.49%; urban growth 1.75%, 2010 Census.

<sup>3</sup> World Bank Public Expenditure Review. June 2011.

<sup>4</sup> In addition to MPW, other recipients of national budget funds are MoH, the Ministry of Environment, and MoHA.

<sup>5</sup> DAK (Dana alokasi khusus) is an annual central budget allocation to most local governments covering 18 sector development requirements. It replaces the previous Inpres (Instruksi Presiden) funds under pre-decentralisation budgets. The total DAK was \$2.5 trillion in 2010 and \$2.7 trillion in 2011. The sanitation component of the DAK was \$40 million in 2010 and \$45 million in 2010 and 2011.

<sup>6</sup> The owner or developer of a domestic or commercial building structure is obliged to provide for sanitary disposal of wastes. Specifications for these facilities are given in regulations, but are not applied in practice. In high urban density areas, use of septic tanks is not appropriate but continues to be practiced.

services in 330 cities.<sup>7</sup> In addition, the Ministry for Public Works has issued *Ministerial Regulation (Permen) PU 16/2008* to support the development of wastewater treatment facilities. The GoI has also enacted *Solid Waste Law 18/2008*, which requires mandatory use of sanitary landfills by 2013.

*sanitation development.*

Fundamental to these policy initiatives is the decentralisation of services as required by law. This is further clarified in implementing regulations.<sup>8</sup> In practice, however, the division of responsibility for sanitation across central and local governments is less distinct. Ministries have assumed responsibility for “lumpy” investments such as treatment plants and major pipe networks, based on the argument that these elements of infrastructure are of national importance.

*Division of responsibility between LGs/GoI has become blurred.*

Lack of accountability in inter-government funding arrangements has been a barrier to expanding sanitation funding for LGs. Until now, concerns about the governance of DAK expenditure have deterred significant increases in DAK funding. The grant channel activated by GoI through the on-granting regulations<sup>9</sup> in 2008 provides accountability for funds transferred to LG through binding grant agreements between MoF and the LGs. This was used effectively by the Water and Sanitation Hibah to channel grants to LGs and to leverage LG investments in water and sanitation. To strengthen the accountability for DAK expenditure by LGs, the GoI is also implementing a pilot program<sup>10</sup> with the World Bank in five provinces. This program reimburses GoI expenditures for verifiable outputs funded by DAK. The successful demonstration through sAIG using similar funding channels with proven governance and accountability measures will assist GoI to channel greater funds to LG for sanitation, leverage greater commitments from LG and redress the imbalance of funding provisions between the central and LG.

*Limitations of DAK and applicability of Grant channel as viable and scalable alternative to LG funding for sanitation.*

### **2.1.1 GoI policies alignment**

The GoI policies and priorities in the sanitation sector are broadly aimed at achieving MDG sector targets. The GoI policy for sanitation is enunciated by MPW in *Ministerial Regulation 16/2008*, which sets out national policies and strategies for the development of domestic wastewater management systems to support Indonesia’s commitment to achieving MDG targets by 2015.

*sAIG aligns with GoI PPSP policy by mobilising LG investments in sanitation infrastructure.*

The key policies are:

- (a) Increasing access to sewerage and on-site sanitation, in urban and rural areas for improvements in public health;
- (b) Institutional strengthening and capacity building of domestic wastewater management personnel.

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<sup>7</sup> PPSP - Percepatkan Pembangunan Sanitasi Permukiman (Acceleration of urban sanitation). The objectives of PPSP by 2015 are to eliminate open defecation by increased sewerage coverage to 5 per cent of urban population in a minimum of 16 cities (includes five cities with new sewer systems); and implementing on-site public sanitation facilities in 226 cities. The five per cent coverage by all sewerage systems is less than 150,000 connections, which translates to services for about 1,750,000 people; this figure is influenced by the 2,000 commercial building connections in PDPAL Jaya with an estimated equivalent population (EP) of 500 each. The PPSP also targets improved solid waste management including recycling in 240 cities, and reduction in flooding of 22,500 ha of land in 100 LGs.

<sup>8</sup> Law 32/2004 (on Regional Autonomy), Law 33/2004 (on Fiscal Balance), and Government Regulation PP38/2007 on the Division of Responsibilities between Government, Provincial Government and Local Government.

<sup>9</sup> Regulations PMK 168 and 169 of 2008 were first applied to on-granting of GoI loan funds for Jakarta’s Mass Rapid Transit. They have been applied effectively in the Water and Sanitation Hibah and Sanitation IEGs under IndII. and are also being applied by GoI for on-granting of national education budget funds. More recently, GoI used the same grant channel for a \$150 million World Bank irrigation loan to finance grants to 110 LGs.

<sup>10</sup> The Local Government and Decentralization Project, loan 7914-ID.

The strategy for these policies is:

- (a) Prioritise organisation of community-based sanitation in densely populated urban slums which are not served by centralised wastewater management systems;
- (b) Gradually transform local systems into centralised sewerage systems in metropolitan and major cities by combining and/or adding to existing systems.

The sAIIIG aligns with and supports this policy by prioritising local government investment in neighbourhood sewerage systems with decentralised wastewater treatment, or construction and connection of neighbourhood sewer schemes to existing centralised sewerage systems.

*sAIIIG encourages LG investment in sanitation infrastructure.*

Gol policy for solid waste is enunciated in the solid waste law which requires local government to operate sanitary landfills by 2013. The MPW has issued ministerial regulations governing solid waste management which include requirements for intermediate treatment facilities (supported by sAIIIG) in addition to requirements for final disposal sites.<sup>11</sup> Emphasis is also given to regional cooperation through the development of multi-jurisdictional waste disposal facilities. IndII is supporting the development of these regional solid waste facilities through its other programs.

*sAIIIG encourages investment in solid waste transfer stations.*

The Gol's key vehicle for service delivery is the PPSP, which broadly identifies the sanitation requirements of LGs through City Sanitation Strategies (CSS) and investment programs.

In related programs, the Government has made poverty alleviation a development priority. The Government's foremost poverty reduction program is PNPM Mandiri, which provides assistance to poor rural and urban communities nationwide through up to three cycles of block grants for improving essential social services and basic infrastructure. The RPJM for 2010–2014 includes PNPM Mandiri as a development tool to accelerate poverty alleviation, with an indicative budget allocation of \$6,754 million over five years for seven PNPM programs.<sup>12</sup> Sanitation is a component of most PNPM programs but many communities do not consider it a high priority. In more recent PNPM programs, MDBs have given higher priority to sanitation and even prepared dedicated sanitation PNPM programs.

*sAIIIG is complementary to other assistance directed at community infrastructure by providing sustainable LG service base.*

## 2.2 Problem analysis

The government of Indonesia faces two major problems: first it must meet the MDGs, which it can do by providing "improved sanitation" facilities to approximately 17% of the population; second, it needs to provide sustainable sanitation services at the city level through investment in sewerage infrastructure.

From one perspective, the sanitation coverage as measured by the percentage of permanent dwellings with a toilet and a septic tank or similar form of treatment is quite high.<sup>13</sup> The problem for LGs and Gol is that this type of installation has become all too prevalent as a means for servicing commercial and institutional buildings, restaurants, and shopping malls in city centres. Local governments have neglected to invest in municipal infrastructure (sewerage) which can provide sustainable sanitation coverage for high density urban development. Historically, LGs have held

*Sanitation coverage in terms of on-site household facilities is high, but provision of municipal infrastructure is low.*

<sup>11</sup> Minister of Public Works regulation No. 21/PRT/M/2006 on national policy and strategy for development of solid waste management facilities (KSNP-SPP).

<sup>12</sup> PNPM programs included in the RPJM are: PNPM Urban (\$664 million); PNPM Rural (\$5,420 million); PNPM Regional Infrastructure for Social and Economic Development (\$132 million); PNPM Rural Infrastructure (\$335 million); PNPM for sanitation - SANIMAS (\$37 million); PNPM for water supply and sanitation - PAMSIMAS (\$469 million); and PNPM Support for Poor and Disadvantaged Areas – SPADA (\$277 million). The Government increased the 2010 allocation for PNPM Mandiri to \$1.3 billion, from \$1.1 billion in 2009.

<sup>13</sup> Reported as 87% in the Susenas survey 2009.

the view that the property owner is responsible for waste disposal and that the LG is only responsible for sanitation facilities that service urban poor in non-permanent or semi-permanent houses. This view has been sustained in part by the availability of funds from Gol ministry budgets which have supplemented, and in many cases replaced, local government expenditure. The default position of most LGs is to spend the DAK allocation on sanitation and little else of their other income, relying on Gol to provide funding for substantial infrastructure.

*Expectation of significant investment from LG is not supported by actual commitments from LG.*

Although the government has put greater emphasis on development of the sanitation sector in the current five-year development budget, problems persist with commitment of funding from local government which are commensurate with ministry budgets. The PPSP project embraces ambitious targets for sanitation investment, a large part of which is expected to come from local government. PPSP estimates an investment of \$8 billion from 2011 to Dec 2015, of which \$5 billion is expected to come from approximately 300 local governments. This is a 30-fold increase over current levels of investment in sanitation by LGs.

*Lack of LG funding due to lack of commitment and lack of subsidies from Gol.*

The main problem facing effective Gol implementation of significant sanitation infrastructure is the lack of local government funding and commitment for investment in their infrastructure. Therefore, while MPW has secured ample budgets to implement central components of sewerage infrastructure, it is constrained by the lack of local government commitment to provide upstream collection sewers and property connections. What is needed is greater commitment of local funds by local government, or more funding to local governments from central government.

Local governments have limited capacity to commit more funds but are still able to do so, since present expenditure on sanitation infrastructure is very low. Providing more funds to local government for municipal sanitation is constrained by the mechanisms available for such transfers. Until now the DAK has been the only channel for such specific fund allocations. However, funding via the DAK is being restricted because of difficulties in the reconciling of DAK expenditure by local government, a problem being addressed by the World Bank and Gol<sup>14</sup>. Furthermore, the Gol restricts the use of the DAK sanitation funds to community-based sanitation programs and does not permit their use in municipal infrastructure programs.

*sAIIIG addressing commitment through incentives and subsidies through support to the grant channel.*

The sAIIIG addresses these two key problems simultaneously. It provides incentives for local government to commit funding for municipal infrastructure, and demonstrates the effectiveness of the grant mechanism as a viable and accountable means of scaling up funding to local government for municipal infrastructure.

### **2.3 Lessons learned**

The Sanitation IEG pilot activity carried out in 22 LGs during Phase I of IndII identified lack of significant funding, fragmentation of programs, questionable sustainability, and poor governance as common problems amongst many of the participating LGs. Investment by LGs in the sector is small<sup>15</sup> compared to other budget expenditure. On average, approximately 1% of the LG investment budget goes to sanitation services. If salaries are included, the figure drops to 0.4% of the LG budget. This means that the average local government spends about \$100,000<sup>16</sup> on sanitation services each year. Most of this budget allocation is for operational

*Lack of LG investment in Infrastructure, fragmentation of programs and poor governance.*

<sup>14</sup> Through the World Bank Local Government and Decentralization Project

<sup>15</sup> Estimates by IndII of all LG expenditure on sanitation are based on extrapolation from the budgets of the 22 LGs. Of that, a smaller fraction is applied to infrastructure.

<sup>16</sup> Excluding DAK.

costs and not for investment in new infrastructure. Despite the commitment to the Gol PPSP policy, there is significant underinvestment in sanitation infrastructure. Other lessons learned point to poor governance in the procurement of goods and services and inadequate oversight of the sector.

Fragmentation of the sector is symptomatic of poor governance and planning. LGs receive small amounts of funding support from a large number of sources.<sup>17</sup> These funds are allocated to *ad-hoc* activities rather than consolidated into mainstream infrastructure components. The fragmentation is compounded by the involvement of more than one LG department (Dinas) in the delivery of sanitation services. More disturbing is the practice of fragmentation of procurement contracts to conform to the ceiling for direct purchase requirements in the procurement regulations.<sup>18</sup> The overall outcome is a lack of focus and a large number of small-scale components mostly linked to the funding source. This lack of consolidation of the sanitation program contributes to poor sustainability in sector development.

*Fragmentation of sector activities at LG is symptomatic of lack of priority by LG and lack of attention to service obligation.*

The proposed sAIG addresses this problem by stipulating disbursement of the grant only for verified outputs of fixed infrastructure. A condition of the sAIG disbursement will be that LG investments are procured through competitive tenders under the prevailing Gol regulations.<sup>19</sup> This will concentrate the funding of the LG into fewer and larger contracts, providing some critical mass in new sanitation service facilities. It will also simplify the oversight of the implementation process, which was a problem in the IEGs.

*sAIG concentrates efforts to infrastructure through competitive tendering.*

The IEGs exposed weaknesses in the capacity of LGs to plan, design, and implement sanitation infrastructure. This was also evident in the implementation of the Sanitation Hibah, which included a component for localised sewer schemes but which was not taken up by any of the five participating LGs. Difficulty with planning and design of these schemes was one of the reasons for the low demand. The sAIG address this through a comprehensive TA plan to review the validity of proposals, designs, and environmental safeguards before committing grant funds.

*sAIG supports capacity development at LG.*

The implementation of the Sanitation Hibah and the IEGs demonstrated strong commitment from LG when support was channelled directly to LG as opposed to Gol support implemented through the technical ministries. The Sanitation Hibah also demonstrated that uptake sanitation services by the community requires more socialisation of the benefits than for other social infrastructure services such as water supply and solid waste management.

*Evidence of strong engagement by LG when grant is given directly to LG instead of indirect programs through ministries.*

The Sanitation Hibah demonstrated that the beneficiaries generally had low demand for improved sanitation, not seeing it as a priority. It was often not identified as a basic need or as having tangible benefits for the family or the wider community. Socialisation of the benefits will be a key component for success of the sAIG. The LG supported by IndII TA inputs will be responsible for the socialisation.

Even when carefully addressed in socialisation activities, and with extensive community participation in planning, decision making and construction, the management and sustainability of communal facilities such as municipal communal toilet and ablution blocks (MCK) is frequently a problem. People often resent having

*Evidence of low sustainability for communal facilities. Opportunity to*

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<sup>17</sup> In addition to the DAK and DBH, the LGs receive funds from the central government via DPDF and PPD (Dana Penguatan Desentralisasi Fiskal dan Percepatan Pembangunan Daerah, based on PMK 118/2010 – a fund for the strengthening of fiscal decentralisation and the acceleration of regional development); DPIP (Dana Penguatan Infrastruktur Dan Prasarana Daerah (based on PMK 113/2010 – a fund for strengthening regional infrastructure and services); and DPPID (Dana Percepatan Pembangunan Infrastruktur Daerah – a fund for acceleration of regional infrastructure development).

<sup>18</sup> Presidential Regulation 54 of 2010 allows contracts of less than IDR 50 million to be procured directly without competitive tendering.

<sup>19</sup> The sAIG will stipulate a minimum contract size of \$50,000 to qualify for the grant.



to pay to use them and clearly prefer the convenience, and privacy, of having toilets in their own house. Reviews of communal facilities have indicated that there is a steady decline in their usage, due in part to households building their own sanitation disposal facilities. However these are often inadequate or discharge directly to drains. For these reasons, sAIG is not supporting the construction of MCK, rather it will promote the construction of neighbourhood sewerage to provide safe disposal of household sanitary waste.

*encourage household toilets and municipal services.*

#### **2.4 Existing AusAID and other donor/multilateral programs**

There are two relevant streams of assistance from donors: (i) assistance to the sanitation sector; and (ii) decentralisation and governance.

The World Bank – WSP is implementing Phase 3 of the AusAID funded WASPOLA facility; delivering sanitation capacity improvements at LG and sub district/village level; and promoting adoption of better hygiene practice by the community through implementation of the CLTS program. WSP secured \$3 million from the Gates Foundation for 2008–10 and is applying for a further \$1.7 million for refinement of the CLTS capacity building efforts within LGs during 2011 and 2012. The sAIG complements these policy and capacity improvements through the provision of grant funds to support implementation of LG programs.

*Waspola provides complementary support on community developed infrastructure.*

The World Bank is implementing the \$22.5 million AusAID funded PAMSIMAS component under WSI, which includes community-based sanitation for approximately 500 villages. The AusAID funded component is part of the IDA funded PAMSIMAS program covering 5,000 villages and peri urban areas implemented as a community based water and sanitation program through DGHS.

*Pamsimas supports rural community based sanitation.*

ADB is financing the Metropolitan Sanitation Management and Health Project (MSMHP) in Medan and Yogyakarta, which will finance downstream sewerage improvements. These will require expansion of upstream tertiary and domestic sanitation infrastructure to feed the downstream expansion. The sAIG will support these upstream developments.

*sAIG can support upstream connections to ADB MSMHP downstream main sewerage.*

The ADB is planning to finance major sewerage investments in five cities where IndII has recently completed Wastewater Master Plans. These will require investment in upstream infrastructure by LGs, and where possible this will be supported through the sAIG also.

*sAIG can support neighbourhood sewerage that will connect to municipal main sewers under WWMP investments.*

The Government of the Netherlands is supporting Gol with the Urban Sanitation Development Program, which provides €10 million for the development of PPSP pipeline projects including CSS. The sAIG will provide support to LGs to implement the pipeline programs.

The World Bank Local Government and Decentralisation Project is supporting strengthened accountability of DAK expenditures through a \$220 million loan which reimburses Gol for good governance and accountability of DAK disbursements<sup>20</sup>. The disbursements from the WB loan are based on LGs achieving prescribed infrastructure outputs (roads, irrigation, water, and sanitation). The LGDP DAK reimbursement project uses the Gol State Finance and Development Supervisory Board (BPKP) to provide oversight verification. The menu of acceptable options for reimbursement under the DAK for communal sanitation includes the type of neighbourhood wastewater systems proposed for the sAIG program, but sAIG will be implemented by LGs rather than community organisations.

*WB DAK accountability strengthening will support community developed schemes.*

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<sup>20</sup> The Local Government and Decentralization Project

In August 2011 the ADB signed a \$100 million loan for Urban Sanitation and Rural Infrastructure Support to the PNPM Mandiri Project, to reduce poverty through community based initiatives to upgrade basic infrastructure in rural villages and improve sanitation services in poor urban neighbourhoods in nine provinces.

*ADB USRIP provides community developed sanitation to complement sAIIIG municipal infrastructure.*

## **2.5 Rationale for AusAID involvement**

The sAIIIG supports the AIP-CS Pillar 1, “sustainable growth and economic management”, through reducing constraints to sanitation infrastructure access and productivity growth. A recent study<sup>21</sup> by the World Bank has shown that Indonesia incurred economic losses of up to 2.3% of GDP due to poor sanitation services. The sAIIIG also supports poverty reduction by focusing on improvements to densely populated low income areas.

Support for AIP-CS Pillar 1 comes in the form of direct benefit to poor households through greater access to improved sanitation facilities and services, and through improved governance and sustainability of these services by LGs.

The sAIIIG will be implemented by Gol using the Gol on-granting mechanism which was established in December 2008 and first used by IndII to successfully deliver the Water and Sanitation Hibah programs. Through IndII, AusAID further tested the “on-granting” mechanism in delivering the sanitation IEG program in FY 2010 and 2011 by IndII. The use of this modality strongly supports the broader objectives of the Paris Declaration and the Accra Action Agenda, as it impacts on:

*sAIIIG focuses on key initiatives to strengthen role of LG under decentralisation in the provision of sanitation infrastructure and services.*

- capacity development of the implementing agencies at Gol and learning from supporting technical assistance;
- delivery through use of partner country systems;
- division of labour among participating stakeholders;
- mutual accountability; and
- ensuring aid flows are more predictable through Funding Agreements at the central level and multi-year on-granting agreements at the LG level.

The sAIIIG complements other AusAID programs in the sector, including the Sanitation Hibah, the sewerage development programs under IndII Phase I, WASPOLA, PAMSIMAS, and indirectly supports health improvement objectives under the AIP-CS.

### **2.5.1 Additionality**

The sAIIIG will focus on support for physical infrastructure. This will shift the balance of spending by LGs from discretionary recurrent expenditure to spending on fixed infrastructure for services. The formula for the sAIIIG will be output-based and will provide an average of 60% of the cost of physical works for new infrastructure<sup>22</sup>. The LG will need to pre-finance the full cost of implementation for a net contribution of 40% after the grant is received. By comparison, the Gol DAK funding requires a 10% contribution from the LG. The proposed 60% grant will leverage LG financing for physical infrastructure to significantly higher levels than LGs are providing now. Pre-financing will also stimulate some LGs to mobilise otherwise dormant financial reserves deposited in Bank Indonesia certificates of deposit. The

*sAIIIG shifts spending to infrastructure. Increases LG contribution to infrastructure from 10% under DAK to 40% under sAIIIG.*

<sup>21</sup> Economic Impacts of Sanitation in Indonesia, WSP – World Bank, 2008 identified economic losses of USD 6.3 billion in FY 2006 due to poor sanitation mostly due to health impacts and pollution of water supplies.

<sup>22</sup> Output-based grants are one form of results based financing in which the payment of grants is contingent on the recipient achieving an agreed outcome. In the sAIIIG, the outcome will be the construction of sanitation infrastructure to an acceptable standard from an approved menu of options for sanitation and solid waste facilities. Grants for sewerage are 67% and grants for transfer station stations are set at 50%.

LGs will continue to finance their obligatory recurring costs. The net result will be an overall increase in the LG sanitation budget with a significant increase in fixed infrastructure investment and a reduction of discretionary recurrent spending. The LGs will be encouraged to consolidate their various discretionary funding sources to invest in infrastructure that qualifies for sAIG financing. Over the course of the program this will result in observable improvements to service delivery by LGs.

The implementation of the program over three consecutive budget years will allow the sAIG to include tests of LG achievement of benchmarks for governance as well as physical investments. The governance benchmarks will be linked to annual reviews while the physical targets will be more flexible. Failure to achieve governance targets will be grounds for review and ultimately suspension of the grant.

*Three year implementation allows for implementation of governance improvements*

### **2.5.2 Partner Agency commitment**

The partner agency, DGHS, actively participated in the Phase I IEG program from design to implementation. During implementation, the DGHS witnessed at first hand the difficulties of supporting sanitation sector development and governance at LG. The partner agency endorses the intent to simplify and rationalise the design of the AIG to an output-based format. DGHS established a team to support IndII during the design progress. Both the Directorate General of Fiscal Balance (DGFB) and Bappenas has supported DGHS in the design of the sanitation sAIG. DGHS also provided budget funds for an operational Central Project Management Unit (CPMU) to oversee the implementation of the Phase I activity and would do so again for the Phase II activity.

*Strong support from partner agencies with the design process.*

Moreover, DGHS and DGFB have demonstrated during the implementation of the Water and Sanitation Hibah and the Sanitation IEGs that they are willing to enforce governance issues arising from LG implementation of the grant programs.

A more critical issue will be the willingness of LGs to adopt governance criteria for continued access to the grants. Evidence from the Hibah and IEG programs show that heads of LGs are willing to take a tough line on services that directly impact the community, especially where the program is high profile and has a visible impact on constituents. The litmus test for the sAIG will be the level of buy-in by LG to the governance criteria and their ultimate performance in meeting the criteria.

The partner agency, the Directorate General of Human Settlements (DGHS), Ministry of Public Works (MPW), is fully committed to the PPSP policy. LGs are committing to the PPSP through their preparation of City Sanitation Strategies. So far this is occurring in accordance with the roll-out schedule of the PPSP. The implementation of the Sanitation IEGs demonstrated strong commitment from Gol and LGs with significant excess demand for this modality of support. Further evidence of Gol commitment to sanitation is the new stand-alone grant under DAK for sanitation in 2010. In FY 2010 the sanitation DAK was \$45 million, up from \$40 million for FY 2009 in parallel with the increased emphasis of programming and budgeting for sanitation through ministry budgets.

### 3 PROGRAM DESCRIPTION

The sanitation AIIG will provide \$40 million in grants over a three-year period to approximately 40 selected local governments for implementing sanitation infrastructure using an “output-based” modality. The sAIIG will provide improved sanitation to approximately 90,000 households or 400,000 beneficiaries. The grants will be defined in an on-granting agreement<sup>23</sup> and the implementation will follow GoI systems and procedures. The LGs will implement the program by pre-financing the works from their own funds and will claim reimbursement after verification of the completed works. Implementation by LGs will comply with the provisions of a Project Management Manual issued by decree of the Director General of Human Settlements and referenced in the on-granting agreements.

#### 3.1 Goal and Objectives

The goal of the sAIIG is to increase the provision of improved sanitation facilities by LGs through the implementation of public sanitation infrastructure.

The project development objectives are to:

- (a) Increase LG investment in sanitation infrastructure that will contribute to meeting the GoI and MDG sanitation service targets by providing up to \$40 million in output-based grants to 40 LGs that are willing to pre-finance \$61 million of sanitation infrastructure during the three-year period 2012–2014.
- (b) Improve governance in the sanitation sector at these LGs by requiring them to adhere to an agreed multi-year sanitation investment program and to make specific incremental improvements in governance.

#### 3.2 Expected outcomes

*What will success look like at the end of the program?* – A successful outcome will be one in which the participating LGs increase their overall sanitation expenditure significantly above non-participating LGs, and where most of that increase is directed to fixed infrastructure investments resulting in increased access, particularly for the poor and vulnerable, to efficient and sustainable sanitation services. The expansion in sanitation services will be accompanied by increased transparency and improved governance in the delivery of these services.

A successful outcome will also be one with evidence that public health and social welfare have improved, and that a socially inclusive approach has been taken. Women, the poor, people with disabilities and other disadvantaged groups, will have equitably participated, including in decision making, and will have enjoyed equitable access to resources and benefits.

#### 3.3 Program features

##### 3.3.1 Entry requirements to the sAIIG program

LGs selected to participate in the sAIIG program will possess three criteria: demonstrated commitment to financing and developing sanitation services; participation in GoI’s Accelerated Program of Urban Sanitation Development (PPSP); and completion of their City Sanitation Strategy.

Evidence of good governance at the LG will also be required, indicated by the absence of negative audit findings by BPK or receiving as a minimum, an unqualified

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<sup>23</sup> The document is a PPH – Perjanjian Penerima Hibah – literally an on-granting agreement signed between the head of LG and the Minister of Finance.

or qualified audit from BPK. Based on preliminary reviews of the implementation of the IEGs, governance at LG is somewhat correlated to BPK audit findings. In addition, if any of the LG's executive or senior staff are known to be under investigation by the KPK, the LG's standard of governance will be deemed unacceptable. Willingness of the LG to commit to progressive governance benchmarks will also be a precondition for acceptance into sAIG.<sup>24</sup> The governance benchmarks will vary from LG to LG since in some locations the local government may have already implemented some of the governance measures proposed. In addition, LGs will be expected to make commitments to socialise the benefits of household sewer connections to the community in general and to women's groups in particular.

#### **Governance Benchmarks**

- Establishment of a Procurement Unit as required under PP54/2010
- Establishment of an UPTD operating authority for sewer schemes
- Establishment of e-procurement and reporting
- Commitment of adequate operational and maintenance budgets

### **3.3.2 Eligible infrastructure**

The menu of sanitation infrastructure eligible for sAIG grant is restricted, and based on an agreed specification for works and unit cost rates; the infrastructure is summarised below and described in detail in Annexe 2.

#### **▪ Wastewater sub-sector**

##### ***(i) Neighbourhood sewerage plus treatment***

These will be simplified sewerage systems, designed for gravity flow only, of shallow depths, less than 1.5 metres, with no manholes or pumping stations but with inspection chambers and inspection openings. Typically each system will serve between 50 and 400 households. Sewers will be limited to two sizes, 100 mm diameter and 150 mm diameter. Connections to the households will include the toilet, bathroom drains, and kitchen sink waste. The local government will be allowed to make its own connection policy. Since the grant will be paid based on the number of house connections made, and not on the construction of the system, there is added incentive to achieve the connections and build larger systems to benefit from the economies of scale. Treatment will consist of an appropriate anaerobic process but will not be prescriptive<sup>25</sup>. Effluent must meet Ministry of Environment requirements. The sAIG will encourage higher effluent quality targets depending on the location and nature of the effluent discharge point. The LG will need to establish a semi-autonomous operating unit, the UPTD, by Year 2 of the project. The UPTD will have the power to collect tariffs and retain the funds for operation. During the transition period, the LG will assign operational responsibility to a Dinas of the LG.

##### ***(ii) Neighbourhood sewerage connected to existing sewerage system***

These will be identical to the neighbourhood schemes connected to treatment except that in cities with existing sewerage schemes, the neighbourhood schemes may connect to the live sewer where treatment will be through the existing facilities. The absence of specific treatment facilities means that a lower level of grant will be paid for each connection to these schemes.

<sup>24</sup> Selection criteria and governance objectives are set out in Annexes 2 & 3 and the Project Management Manual.

<sup>25</sup> Imhoff tanks, upflow anaerobic reactors, multi compartment septic tanks. Effluent treatment may include absorption through soil or cultivated wetland.

- **Solid Waste sub-sector**

**(i) Intermediate Solid Waste Transfer Facilities (SPA)**

Intermediate Transfer Facilities, *Stasiun Peralihan Antara (SPA)*, receive solid waste collected by small trucks from various sources including domestic areas, interim collection stations, and recycling depots. They aggregate and compact the waste, which is then hauled to the final disposal site by a fleet of large trucks. These facilities may vary in size from 400 m<sup>2</sup> to more than 1,500 m<sup>2</sup>. Therefore the sAIG does not pre-assign a unit cost for these facilities; rather each proposal will be reviewed, and assessed in terms of readiness for implementation. At that time agreement will be reached on the appropriate cost for the facility and the grant will be fixed at 50% of the agreed cost. The grant will then be paid on satisfactory completion of the works. The solid waste interventions may be delayed into Year 2 of the program to better assess the sector.

**3.3.3 Levels of grant**

The grants for each type of infrastructure component will be predetermined on a scale between 67% and 50% of the total cost of construction, depending on the type of works. Higher grants are allocated for Simplified Sewerage Systems at 67% of nominal cost, while solid waste Transfer Stations will receive a 50% grant. The different levels of grant are intended to direct LG sanitation activities towards the more sustainable components.

**Preliminary Level of Output-based Grants for Eligible Components**

	Unit of payment	Fixed Price Rp	Level of Grant	Grant per family Rp
<b>Wastewater</b>				
1.1 Neighbourhood Sewerage System and Treatment Plant connecting minimum 50 families to treatment plant connection		6,000,000	67%	4,000,000
1.2 Neighbourhood Sewerage System connected to Existing Wastewater System extending and connecting new customers connection		4,500,000	67%	3,000,000
<b>Solid Waste</b>				
2.1 Intermediate Transfer Station (SPA) minimum 1,000m <sup>2</sup>	Subject to prior review and agreement on cost installation		50%	

**3.3.4 Implementation**

In executing the sAIG program, local governments will apply the DGHS Project Management Manual. Implementation of the Simplified Sewerage Systems will comply with DGHS standards, specifications and technical guidelines. The sewerage systems will be constructed by qualified contractors procured through competitive bidding under prevailing GoI procurement regulations. An Implementation Consultant will support the LGs in the detailed design and contract supervision.

**3.3.5 Verification**

An independent Verification Consultant will inspect the completed works in the field, check the LG's progress towards governance benchmarks, and calculate the value of grant payment due. The Consultant will identify any shortfalls in quality or quantity of infrastructure constructed and recommend either remedial actions, or non-disbursement for the non-qualifying component. Failure by the LG to achieve satisfactory progress on governance will trigger a review of the grant agreement; continued governance failures will lead to cancellation of the grant.

### **3.3.6 Program management**

DGHS will be the principal partner agency responsible for execution of the program, although DGFB and BAPPENAS have also been involved with AusAID / IndII in the program design. DGHS, in close consultation with IndII, will have primary responsibility for selection of the LGs, approval of their proposed programs and allocation of the grants. DGHS will then propose the selected LGs and grants to DGFB for award of the on-granting agreements. AusAID / IndII will work with DGHS and DGFB to prepare the Direct Funding Agreement, the Project Management Manual, and the content of the on-granting agreements. DGHS will issue the Project Management Manual by decree of the Director General and will establish a Central Program Management Unit to be responsible for oversight of the sAIG program.

IndII will engage consultants to support DGHS with program appraisal, baseline and other surveys, detailed design, implementation oversight, and independent verification. DGHS will be responsible for preparing recommendations for grant payment, which will be subject to a *No Objection* from AusAID / IndII. DGFB will manage the sAIG funds as part of their national budget and authorise payments through the Special Account at BI, and report on the use of the funds to AusAID.

### **3.3.7 Land acquisition, social and environmental issues**

In order to avoid delays due to land acquisition, any land required for construction of the sanitation infrastructure must already be in the ownership of the LG or the local community prior to sub-project approval. The land must also be free from any settlement or buildings which would delay implementation.

The sAIG's effectiveness and sustainability will be increased by ensuring a gender inclusive approach is adopted and that women's, as well as men's, needs and priorities are heard. Socialisation and information dissemination will be designed to reach both women and men and there will be equitable participation by women and men in all aspects of sAIG. The project will promote disability inclusive development, ensure equal access to infrastructure for people with disabilities, and facilitate active participation by people with disabilities in project activities.

It is expected that some PPSP activities will have already required a Strategic Environmental Assessment to ascertain whether the plans comply with Indonesian standards and safeguards. LGs are responsible for ensuring that all required environmental safeguards have been prepared (AMDAL, RKL, RPL); DGHS will review them as part of the approval process. In most cases sAIG sub-projects will be small-scale with the potential to cause local, short-term, negative social and environmental impacts which will be addressed during the detailed design.

### **3.4 Form(s) of aid proposed**

Three alternative approaches were considered: (i) channelling the funds through the technical ministry, MPW; (ii) a DAK type project with possible enhancements; and (iii) an output- or performance-based grant to the LG.

Channelling of the funds through MPW would mean that MPW would provide indirect sanitation improvements to communities by implementing them through the provincial program manager. This runs counter to the current decentralisation objectives which are to enhance the transfer of funds for sanitation to LGs. The MPW budget is already at the limit of MPW capacity to implement, and no further consideration was given to channelling funds via MPW.

Examining the DAK concept as an option raises other issues. The DAK is in the form of a budgetary entitlement to LG. This would mean that the grant would be passed

on to the LG as a budget allocation for the LG to spend and for Gol to subsequently report expenditure to AusAID. This modality has high risk and the governance mechanisms are not in place to allow its consideration.

Nevertheless the WB Local Government and Decentralization project has many good features and its implementation should be monitored to examine possible cross fertilisation of methodologies and approaches with the grant mechanism.

A significant improvement on the DAK model is the non-output based (conventional) grant mechanism which requires LGs to sign a binding grant agreement which can be enforced with penalties for non-compliance. This has better governance provisions than the DAK but also requires considerably more implementation oversight and obligatory prior review of supporting documents for all payments. The Gol is using this modality for education grants and other central grant transfers.

A hybrid of this modality combined with performance assessment was used for the IEGs. The complexity of implementing the IEGs confirmed that this level of oversight and supervision of the implementing agencies can be a limiting factor in its use. It also exposed weaknesses at LG in service delivery and governance in the sanitation sector.

As a result of this assessment and the lessons learned from the IEGs, the preferred approach for delivery of the sanitation AIIG is the Gol grant channel using an output based modality, as has been used successfully in the Sanitation Hibah<sup>26</sup> during Phase I of IndII.

### **3.5 Estimated program budget and timing**

#### **3.5.1 Project pipelines and readiness in 2012**

Preliminary overview on sanitation program for year 2012 has been obtained from 24 LGs during the socialisation of the sAIIG. Those LGs were selected from previous IEG program, LGs assisted by IndII in preparing WWMP and other LGs proposed by DGHS that had a suitable 2012 sanitation program. Six of these LGs have programs for the construction of neighbourhood sewerage systems and the others are for additional house connections, totalling about IDR 42 billion or equivalent to \$ 4.7 million in grants. A total of IDR 1.26 billion or equivalent to \$0.13 is to be budgeted for solid waste sector (Transfer depot) The DEDs for 2012 programs have either been prepared, are in process or, will be prepared at the beginning of 2012. Six LGs have completed their DEDs. Land is reportedly available or in preparation.

#### **3.5.2 Governance benchmarks**

It is likely that the first year program will contain readily achievable governance benchmarks to help establish relationships and provide confidence to LGs, with more onerous governance criteria in subsequent years. Implementation arrangements and the level of funding support will be defined in a Funding Agreement between Gol and AusAID.

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<sup>26</sup> The Sanitation Hibah is an output-based grant program in which the LG invests equity in a sewerage operating authority which in turn applies those funds in addition to its own funding to expand sewerage connections. The grant is then disbursed to the LG based on evidence of new sewer connections having been made in accordance with agreed specifications and recipient targeting. The application of the sanitation hibah is limited to existing sewer schemes with operating sewer authorities.



### 3.5.3 GoI PPSP schedule

The GoI PPSP initiative covers 330 cities. The roll-out of the PPSP is expected to be complete by 2014 as shown in the table below. It is anticipated that the sanitation AIIG could cover up to 50 LGs over a three-year period, allowing six months start-up and six months for completion and exit.

### 3.5.4 Uptake of the grant

Although the grants will be awarded for three years there will be an annual review and verification of the qualifying program for the current budget year. The anticipated uptake of the sAIIG is shown below.

#### Uptake of the Grant and Disbursement to GoI Special Account

AusAID FY	2011-12	2012-13	2013-14	2014-15	
GoI FY	2011	2012	2013	2014	2015
CSS Complete	114	176	248	330	Final verification and closure
IndII sAIIG LGs	start	30	40	50	
Current LG Inv*. \$ mil		3	4	5	
sAIIG \$ (mil)	start	4	20	16	
Disbursement to BI account		10	15	15	

\* excluding operating expenditure and salaries

In Phase I, the IEG program provided an average of \$250,000 to each LG for essentially a one year implementation period. In Phase II, the inclusion of small scale sewerage will increase the grant size to approximately \$400,000 for each LG, each year. The application of the program over multiple years could result in average grants \$1.2 million for each LG over three years. There will be 114 LGs that would qualify for the sAIIGs by the end of 2011. These are the 65 existing LGs with CSS and the 49 additional LGs with CSS in preparation during 2011. The LG selection and grant allocation criteria will aim to arrive at about 20% of qualifying LGs progressively entering the program during this period. Based on these figures a total sanitation AIIG allocation of \$40 million over 3 years would leverage approximately a 400% increase in delivery of new fixed sanitation infrastructure by the participating LGs.

The sAIIG will also include a public diplomacy and communications component. Implementation of the Water and Sanitation Hibah has demonstrated that this is an effective tool in emphasising the constituency benefits of the program to the heads of LGs.

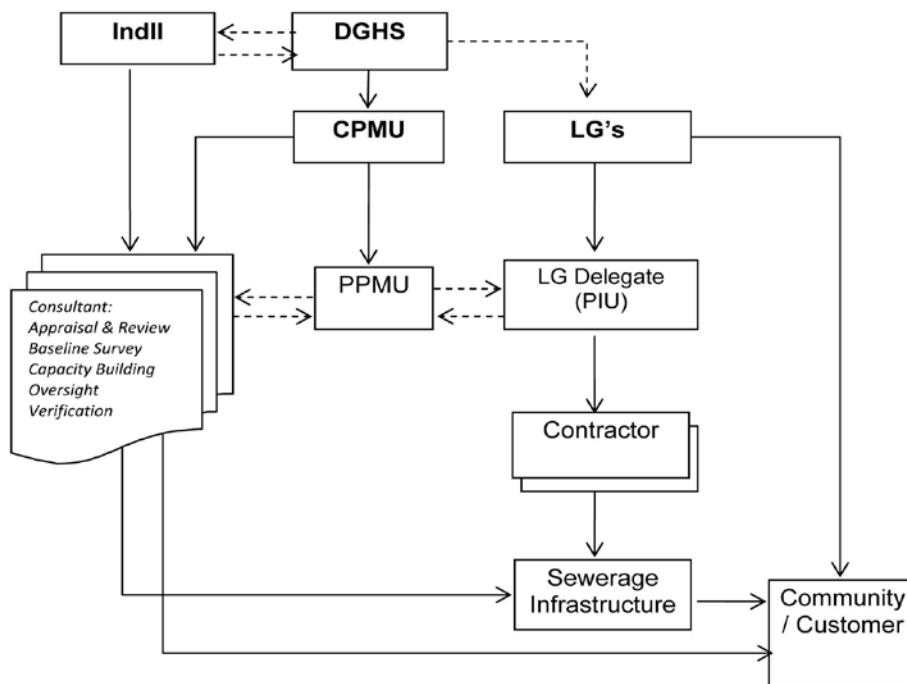
## 4 IMPLEMENTATION ARRANGEMENTS

### 4.1 Management and governance arrangements and structure

The program governance, management and organisational structure is shown in more detail in Annexe 3 – Program Management and Implementation Arrangements.

#### 4.1.1 Management structure and organisation

At the Central Government level, the sAIG program will be managed by a special purpose coordination unit established by decree of the Directorate General of Human Settlements. The coordination unit will consist of Steering and Technical Teams, operating through a Central Project Management Unit (CPMU) in DGHS, and supported by Provincial Project Management Units (PPMU). The CPMU will be responsible for sAIG program administration and will have a wide range of responsibilities, including: coordination with other government agencies, selecting LGs to participate, appraising LG multi-year sanitation programs, approving annual qualifying programs, reviewing sub-project designs, monitoring the LGs' procurement processes, monitoring and reporting on physical and financial progress, checking construction quality, verifying completed works, approving grant claims, and monitoring and evaluation. Consultants procured by Indll will support the CPMU by providing technical assistance in: oversight, sanitation program appraisal, review of qualifying programs, baseline surveys, and independent verification and monitoring.

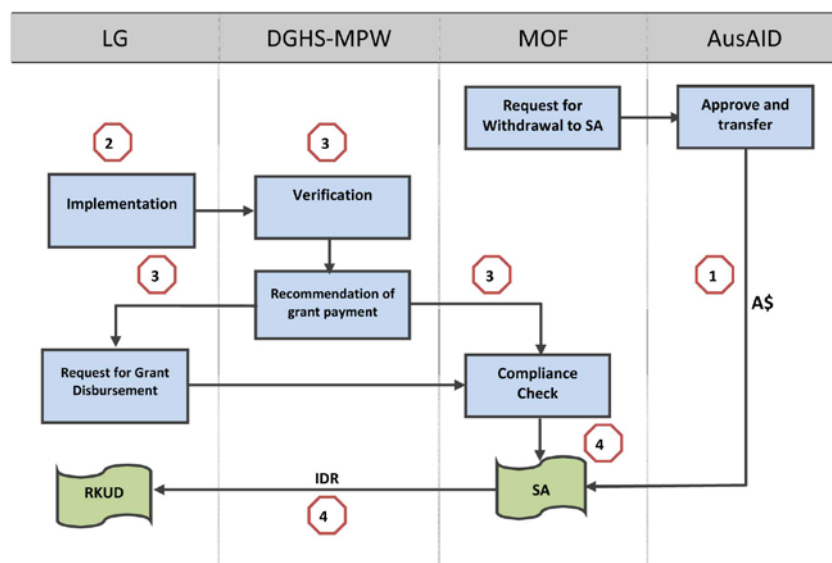


At the Local Government level, Project Implementation Units (PIU), together with Local Task Forces (SKPD), will be established by decree of the Head of each participating Local Government. The PIUs will be responsible for project implementation and will have a wide range of responsibilities, including: preparation of sanitation programs, preparation of detailed designs and bidding documents, procurement of contractors, raising community awareness and social

marketing of sAIG, construction supervision and management, enforcing construction quality requirements, reporting physical and financial progress, and preparing documentation for grant payment applications. Consultants procured by IndII will support the PIU in discharging these duties. The technical assistance they provide will include: review and completion of detailed designs and contract documents implementation oversight and capacity building to support LGs in building community awareness, social marketing, procurement development and delivery of sanitation services.

#### 4.1.2 Fund channelling

The sAIG program will be implemented through Gol systems and procedures, as shown in the figure below. A direct funding agreement will be signed by Gol and AusAID, following which Gol will establish a Special Account in Bank Indonesia (BI).



- (1) The grant funds are transferred to the Gol Special Account following a request from MoF to AusAID.
- (2) The LGs implement the qualifying program works in accordance with the Grant Agreement between them and MoF.
- (3) MPW verifies the completion of the works and issues a recommendation for the amount of the grant payment due; LG submits a request for a grant disbursement to MoF.
- (4) MoF checks the documentation for compliance with the Grant Agreement and Project Management Manual and then transfers the funds from the Special Account to the LG's general revenue account (RKUD).

#### 4.1.3 Indirect disbursement and currency management

Recent changes within Gol prevent BI from making direct disbursements to LGs. This is now done through an intermediary government bank. One possibility to consider is whether it is feasible to establish dual IDR and \$A accounts at BI to flexibly manage currency exchange rates. The possibility of rolling over residual funds from the IEG program to the AIG is also a matter to be considered.<sup>27</sup>

<sup>27</sup> At present approximately \$300,000 is identified as non-qualifying expenditure and an additional \$150,000 credit from exchange rate gains.

## **4.2 Implementation plan**

The sAIG program is planned to run for three years from early 2012 to the end of 2014, with each year following a common annual activity cycle. Preparation of the sAIG program began in September 2011 and final verification, evaluation and grant disbursement will be completed by June 2015.

Program preparation activities already underway include: collecting information about the existing DAK and SANIMAS programs, reviewing previous similar sanitation projects for lessons which can be learned about creating sustainable infrastructure, designing the sAIG program and preparing this PDD, establishing LG selection criteria, socialising the sAIG to LGs to generate interest and encourage them to start their preparations, and preparing the Project Management Manual with DGHS and DGF. Socialisation efforts were vital because, as the sAIG program is output-based, if any works are to be implemented in 2012 the LGs need to fully fund them in their 2012 APBDs which are prepared in October / November 2011. These budgets then have to be approved by the DPRD, which can be a long process.

LGs will join the program in annual batches once they have satisfied the qualifying criteria. Consequently, some may participate in sAIG for three years, some for two years, and possibly some only in 2014. The target is for 40 LGs to participate, but the final number will be dictated by the availability of uncommitted grant funds, which will depend on the extent of the sanitation programs proposed by the LGs and their success in completing eligible works.

No.	ACTIVITY	PARTIES INVOLVED	2011	2012				2013				2014				2015			
			4	1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16
<b>I. PREPARATION STAGE</b>																			
	FY 2011 Revise SA & MoF Agreement	IndII, AusAID,MoF	●																
	sAIG - Project Design Document, Project Manual,Peer Review &agreement	IndII, AusAID,MoF,DGHS,Bappenas	●																
	sAIG Program 2012 listed in APBDs & Appraisal	LGs																	
<b>II. IMPLEMENTATION STAGE</b>																			
	FY 2012 Appraisal of FY 2012 LG Programs	IndII, DGHS,LGs		■															
	PPH Preparation & Signing	MoF		■	■														
	Establish Special Account at BI & first Transfer	DGHS, IndII			■	■													
	Recruitment of Consultants first Sub Project for TA, Baseline Survey and Verifications	DGHS, IndII			■	■													
	Construction	LG				■	■												
	Verification	PPMU, PIU,LGs,IndII					■	■											
	sAIG Disbursement	DJCK,MoF					■	■											
	Review Progress and Reallocation of Grant	DGHS, IndII, MoF					■	■											
	Monitoring	DGHS, IndII					■	■	■										
	Socialisation and Selection of Next batch (2 & 3)LGs	DGHS, IndII				■	■												
	FY 2013 Review and Appraisal of FY2013 LG Programs	DGHS, IndII						■	■										
	Recruitment of Consultants Second Sub Project for TA, Baseline Survey and Verifications	DGHS, IndII							■	■									
	Construction	LG								■	■								
	Verification	PPMU, PIU,LGs,IndII									■	■							
	sAIG Disbursement	DGHS,MoF										■	■						
	Review Progress and Reallocation of Grant	DGHS, IndII,MoF											■	■					
	Monitoring	DGHS, IndII												■	■				
	FY 2014 Review and Appraisal of FY2014 LG Programs	DGHS, IndII													■	■			
	Recruitment of Consultants Second Sub Project for TA, Baseline Survey and Verifications	DGHS, IndII														■	■		
	Construction	LG															■	■	
	Verification a	PPMU, PIU,LGs,IndII																■	
	sAIG Disbursement	DGHS,MoF																	
	Monitoring	DGHS, IndII																	

Once formal approval for the sAIG program has been received from AusAID, the LGs will be invited to submit their proposed sanitation programs. IndII will recruit Appraisal Consultants who will support DGHS in determining whether the LGs qualify for participation, whether their proposed programs satisfy grant requirements, and whether the LG can fund the programs. Appraisal will include visits to the LGs to discuss their programs, collect information and determine their willingness to meet governance criteria. Once DGHS is satisfied with the LG's program they will notify DGFB of the grant proposal.

Successful LGs will then begin the annual sAIG activity cycle by preparing detailed designs and bid documents for their first year program, supported by the Program Preparation Consultant. These documents will have to be approved by DGHS before they can be tendered. In the meantime, consultants will conduct the Baseline Survey at each sub-project location. Formal grant notification should be received from DGFB by May, and tendering will then begin. Construction is expected to begin in July and to be completed in about four months. Within two months of commissioning each sub-project, the Verification Consultant will make a field inspection and determine the quantity of eligible infrastructure which has been satisfactorily completed. This determination will be used by DGHS to calculate the amount of grant money payable. Grant payments should be authorised by the end of January and the LG should receive the grant by the end of March, allowing them to recycle the money in their second-year sanitation program, if they wish. The second-year program will follow the same annual cycle as the first.

### **4.3 Technical assistance plan**

Comprehensive technical assistance to support DGHS, the participating LGs, and IndII in the successful delivery of the grant program is included in the project design. DGHS will establish a CPMU to administer the program. The CPMU will require TA support in appraisal, approval, oversight, monitoring and reporting, while IndII will also require support in fulfilling their responsibilities. Local governments are required to plan, design and implement infrastructure with which they are not familiar, and for which they have very limited technical and human resource capacity. The scope of technical assistance anticipated for the project is described in the following sub-sections. The optimum way to package these services into consultancy contracts will be decided once the locations of the participating LGs are known.

#### **4.3.1 Program appraisal and review**

Initially the Consultant will appraise the multi-year sanitation programs proposed by candidate LGs as part of the selection process, including their planned budget allocations and governance indicators. Once LGs have been accepted into sAIG, the Consultant will review each LG's annual program and confirm compliance with environmental and social safeguards, land acquisition and relocation, procurement documents, and other requirements of the Project Management Manual and Grant Agreement. The Consultant will support the CPMU in determining the qualifying programs for each year's implementation; sAIG funds will only be disbursed for infrastructure that qualifies.

#### **4.3.2 Baseline survey**

The Consultant will conduct a baseline survey of the qualifying programs for each year. The scope of work will encompass the collection of baseline data on the target populations in each selected sub-project area through a census of household size, socio-economic status, sanitation behaviour and interest in becoming a customer.

The survey will also collect information on LG sanitation budgeting and governance as a basis for assessing progress over the life of the project.

#### **4.3.3 Program preparation**

The Consultant will support the CPMU in administering the sAIG program and will be responsible for ensuring that LGs are adequately prepared to implement their sanitation programs. The Consultant will review existing designs and documents and, where necessary, complete the detailed designs and tender documents. The Consultant will ensure that there is a pipeline of sub-projects being prepared by LG for implementation in subsequent years.

#### **4.3.4 Capacity building and community awareness**

The Consultant will provide capacity building for the new UPTD-PAL which will become responsible for design, construction supervision, and the operation and maintenance of the new sAIG wastewater systems, as well as having responsibility for all existing wastewater services of the LG. The Consultant will also provide capacity building to the LG's procurement staff as it establishes the new Procurement Unit.

An important capacity building tasks will be supporting the LGs to design and prepare materials for community awareness raising and developing a strategy for social marketing which reaches both women and men, to generate interest in, and demand for, the proposed new sanitation services. The strategy will be aimed at changing people's health and hygiene habits and behaviour, as well as educating them in the health risks associated with untreated sewage. LGs are encouraged to appoint their own facilitators to implement community activities, in particular awareness raising and social marketing.

The Consultant will ensure that the capacity building team includes social/poverty and gender specialists to support LGs in developing socially inclusive and gender sensitive approaches for implementing sAIG activities. Related tasks will include illustrating the benefits of ensuring women participate equally with men, gender issues faced in the field, and how to ensure that women participate.

#### **4.3.5 Oversight**

Working in close association with the CPMU, the Consultant will be engaged early in the program and will provide quality assurance and technical oversight of the implementation process from the tender stage to completion and handover of the works. However, the LG will be responsible for day-to-day supervision of their contractors.

#### **4.3.6 Independent verification**

The Consultant will be responsible for compliance verification of the completed works with the: Detailed Design, Technical Specifications, Project Management Manual, Grant Agreement, and prevailing procurement regulations. The Consultant will verify the volume of eligible infrastructure constructed and also collect the data required for monitoring and evaluation.

## SAIIG IMPLEMENTATION PLAN

2011	2012		2013		2014		2015
S-1	S-1	S-2	S-1	S-2	S-1	S-2	S-1
Criteria preparation	Implementation FY 2012:		Implementation FY 2013:		Implementation FY 2014:		
1) LGs to access sAIIG	procurement	implementation	procurement	implementation	procurement	implementation	
2) Component activities for sanitation in accordance with grant req'mts			Evaluation 2012		Evaluation 2013		Evaluation 2014
Selects 1 <sup>st</sup> batch of LGs that meet the above requirements		Select 2 <sup>nd</sup> batch of LGs that meet with criteria & req'mts	Select 3 <sup>rd</sup> batch of LGs that meet with criteria & req'mts				Evaluation, review measurement of output outcome.
Assist LGs to develop 3-year program planning for 2012 till 2014	Appraisal of 2012/ 2013/ 2014 Program, verify DPA 2012	Appraisal of 2013 and/or 2014 Program		Appraisal of 2014 Program	Assistance to Gol in preparing grant scheme for the upcoming years		Exit Strategy
Grant Award 1 <sup>st</sup> batch	PPH Process 1 <sup>st</sup> batch	Grant Award 2 <sup>nd</sup> batch	PPH Process 2 <sup>nd</sup> batch	Grant Award 3 <sup>rd</sup> batch	PPH Process of 3 <sup>rd</sup> batch		Total PPH= 40
	Review criteria of waste water and solid waste components.		Verification for 1 <sup>st</sup> batch payment Verification of DPA 2013	Grant payment	Verification for 2 <sup>nd</sup> batch payment Verification of DPA 2014	Grant payment	Verification for 3 <sup>rd</sup> batch & grant payment
	Prepare LGs for 2013 & 2014						
Governance Targets	Modest		Realistic		Ambitious?		



#### **4.4 Verification**

The verification process will consist of two distinct stages. Once the grant has been awarded and defined in the on-granting agreement, the LGs will have also agreed to an outline implementation plan. However, the commitment of funds to specific components will require a verification of: (i) acceptable planning including land acquisition, social and environmental safeguards; (ii) acceptable design; and, (iii) acceptable procurement documents. This verification will be the responsibility of the CPMU assisted by IndII consultants. Prior approval of individual components will be required for LGs to qualify for a grant. Once the infrastructure has been implemented, the LG will request verification (post review) by the CPMU. Consultants from IndII will initially assist the CPMU. During the first year, the BPKP will witness the verification for payment of the grant. The role of the IndII verification consultant will progressively reduce during the second and third year of the program while that of the BPKP will increase. By the final year of the program, the verification process should be a GoI procedure with the IndII consultant providing a supporting role only. The roles and responsibilities of the DGHS (CPMU) and the BPKP in the verification process will be progressively developed during the first two years of implementation.

#### **4.5 Monitoring & Evaluation plan**

M&E for sAIIIG will be aligned with the broader IndII Phase II M&E framework for Watsan where end outcomes and objectives have already been defined. The development objectives for this activity are:

- (a) Increasing LG investment in sanitation infrastructure that will contribute to meeting the GoI and MDG sanitation service targets.
- (b) Improve governance in the sanitation sector at these LGs by requiring them to adhere to an agreed multi-year sanitation investment program and to make specific incremental improvements in governance.

M&E for sAIIIG will comply with the annual activity cycle. Aside from on-going monitoring of program inputs and outputs, sAIIIG will comprise a sub-project appraisal process, baseline study and analysis, implementation oversight, project verification and post-project evaluations. Annexe 5 provides more detail on the steps indicated.

M&E will be carried out by several parties, including GoI (CPMU, PPMU, PIU) and independent third-party Implementation and Verification Consultants that will be recruited under the program. GoI will be responsible for routine M&E activities consistent with current DGHS guidelines for sanitation infrastructure programs. IndII consultants will provide relevant support to these efforts, such as undertaking specific activities to assess progress toward meeting key program outcomes and other aspects of program implementation (gender, access, etc.) of specific interest to AusAID.

The program design matrix outlines a series of outcomes (short, medium and long) that will form the basis of reporting over the life of the program. The structure of the outcomes means that evidence of progression towards outcomes can be justified and the verification of connections demonstrates causal linkages to the investment provided through IndII. The outcomes will form the basis of reporting and will also allow for modifications to occur during the life of program if an outcome is unattainable or needs to be refined due to changes in the external environment.

The outcomes are structured to be quantifiable and have appropriate indicators. The most important outcomes relate to the provision of sanitation infrastructure that meets the standards and requirements of Gol. Other outcomes centre on improvements at the LG level with regards to sanitation planning, budgeting and governance, as well as the adoption of poverty and gender sensitive approaches to the implementation of relevant sanitation activities.

Indicators have also been defined and included as part of the design. The indicators will be reviewed annually to ensure they remain consistent, targeted and relevant to the needs of the program and are providing the necessary information to both Gol counterparts and AusAID.

Annexe 5 provides in-depth details on the monitoring arrangements. In short, monitoring will occur at two levels – the first will be the implementation of sanitation infrastructure and the second will focus on the broader support provided to LGs. IndII M&E reporting templates will be utilised for the monitoring of activities. Exception reporting will also be utilised in the event of immediate issues requiring attention.

#### **4.6 Communications**

The template for the sAIG's communications and public diplomacy program will be that used for the WSI Water Hibah in 2011. As with the Water Hibah, the sAIG program will identify and communicate a number of key messages, depending upon the target audience. At the community and household level, the message will focus on the social and economic benefits of proper sanitation facilities and will address the sometime indifferent attitudes toward sanitation, evidenced within lower income areas. At the local government level, the message will emphasise the high political returns to local leadership from increased LG investment in, and commitment to sanitation services. At the central level, the message will focus on the benefits of devolving implementation to local government as the best means of achieving ambitious coverage targets while retaining management and oversight as a central responsibility; this being the most effective way of improving sanitation outcomes at the local level.

Various modalities will be used to deliver these messages, and may include the use of:

- events/ceremonies at both the district/city and community level attended by local/community leaders, other stakeholders and beneficiaries at the completion of construction;
- education/socialisation programs at the village/community level;
- production and release of material for print media (e.g. photos, press releases, human interest stories, profiles on household beneficiaries, etc);
- radio talk back and features, and television (if feasible);
- signage – stickers, signs, banners, etc;
- documentary videos for upload to the IndII website, YouTube and other purposes; and
- commemorative publications (such as coffee table book , calendars etc).

Important lessons can be drawn from the success of the WSI Water Hibah public diplomacy program, particularly with regards to the frequency and sequencing of events, and these will be incorporated into the sAIG's communication plan developed in the early months of implementation.

#### 4.7 Procurement arrangements

Public procurement in Indonesia has traditionally been conducted based on regulations which have been updated and modified from time to time. Unlike the procurement guidelines of the Multilateral Development Banks that stress the principles of economy, efficiency and transparency, these decrees have always had multiple objectives reflecting the varying emphases of Government policy.

International donor efforts at procurement reform resulted in the Paris Declaration on Aid Effectiveness (2005), Accra Agenda for Action (2008), and the Jakarta Commitment: Aid for Development Effectiveness – Indonesia’s Road Map to 2014 (2009) under which donors agreed to align their programming cycles with those of Government of Indonesia systems and increasingly to use Government of Indonesia’s financial management, procurement, monitoring and evaluation, and reporting systems. The Paris Declaration and Accra Agenda for Action are based on the premise that by working with government systems donors are increasing the effectiveness and efficiency of those systems, addressing the systemic causes of poor service delivery.

Procurement reform in Indonesia resulted in *KepPres 80/2003*, which had many weaknesses and was open to multiple interpretations, being replaced by *PerPres 54/2010*, which is intended to be followed by a separate Procurement Law covering all public funded expenditures. Meanwhile, *PerPres 8/2006* introduced the concept of establishing procurement units (ULP-Unit Layanan Pengadaan) in every government agency at every level, but gave no timeframe; *PerPres 54/2010* set a deadline of 2014. ULPs are intended to be pools of professional procurement officers which will take over the role of the current *ad hoc* tender committees. *PerPres 54/2010* clearly makes mandatory the use of national procurement systems for channelling external funds - also a part of the Jakarta Commitment in 2009.

The sAIG program will align with various national and international procurement reform initiatives that have been established in recent years, including the Paris Declaration on Aid Effectiveness (2005), Accra Agenda for Action (2008), and the Jakarta Commitment: Aid for Development Effectiveness – Indonesia’s Road Map to 2014 (2009). It will also follow the provisions of *PerPres 54/2010* and use existing Gol on-granting regulations PMK 168 and 169 of 2008 to disburse grants directly to LGs, through MOF. These channels provide accountability and have been applied successfully in the Water and Sanitation Hibah and sanitation IEGs under IndII. The flow of funds is described and shown in detail in Annexe 3.

The Gol legislation mandates that the Implementing Agency DGHS take responsibility for the oversight of the application of the grant funds. Technical Assistance from IndII will include provision of Appraisal, Implementation and Verification consultants to assist DGHS with their oversight duties and support the LGs. The TAs will include the support required to verify compliance with the grant agreements and the technical standards of the Implementing Agency (DGHS). Consultant services will be procured by IndII through select tenders from qualified firms in the consultant pool.

sAIG is an output-based program and LGs are therefore required to pre-finance all construction works, reducing the procurement risks for AusAID. LGs will be required to package the sub-projects and tender them in accordance with *PerPres 54/2010*. The practice of packaging works into small contracts to avoid having competitive tenders will not be permitted and the entire procurement process will be subject to post-review. The grant eligibility, detailed design, procurement and construction quality of sub-projects will all be monitored and supported by the sAIG consultants.

On completion and commissioning of the sub-projects the independent verification consultants will determine the quantity of operational infrastructure; in the case of wastewater systems this will be the number of new house connections installed. Grant funding will follow the criteria and allocations described in Section 3.4 and will be based on the fixed prices shown, not on the actual tender prices obtained by the LGs. This will help to insulate AusAID from the cost of any malpractice in the tender process, as the additional cost of any inflated prices will be borne by the LG.

#### **4.8 Sustainability issues**

Sustainability of sanitation infrastructure and services is a key concern in the design of sAIG. It is well-known that facilities implemented under community driven modalities have often had poor levels of sustainability in Indonesia. This has been confirmed by a recent survey for DGHS of 41 community implemented sanitation facilities constructed between 2008 and 2009.<sup>28</sup> The survey found that 17% were operating very well, while 32% were operating well but with lower than the planned number of users; 52% were either incomplete, or partially or completely non-operational.

The sAIG design is therefore focused on neighbourhood, simplified sewerage schemes, implemented by local governments using their own funds. After completion and handover, these assets will go onto the local government register. The use of good quality designs and materials implemented by qualified contractors procured competitively and overseen by IndII supported TA should produce sanitation infrastructure which has a reasonably long service life.

The requirement for LGs to establish a Technical Service Unit for Wastewater Management (UPTD-PAL) in the first year of the project will further strengthen sustainability of service delivery and maintenance of the facilities. The UPTD-PAL will be expected to eventually develop more autonomy, either as a Local Government public service agency (BLUD) or a Local Government owned wastewater company (PD PAL).

Sustainability will be a focus of post-project evaluation that will seek to verify continuation of sanitation prioritisation, good governance practices, sound management and maintenance of facilities. All of these will contribute to the longer-term goal of meeting national and international targets for access to efficient, sustainable and equitable sanitation services.

#### **4.9 Overarching policy issues including gender, anticorruption, environment and child protection**

Poor environmental sanitation is a symptom of poverty but also causes and exacerbates poverty. Inadequate sanitation, solid waste management and drainage are more likely to be experienced by people living in low income communities. They are more likely to be living in areas subject to inundation, where infrastructure is poor and they have the least power to influence decision making which could improve their situation. Poor environmental sanitation has economic costs for individuals, households, the community and the nation as a whole. For people who are already poor or near poor, the financial cost of inadequate environmental sanitation can push them further into poverty.

GoA has a poverty framework which aims at reducing the incidence and severity of poverty in the Asia Pacific region through its aid program. Areas of the poverty framework particularly relevant to the implementation of the sAIGs are: to provide

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<sup>28</sup> Draft Final Report of SANIMAS Monitoring Program 2008-2009 by PT Waseco Tirta (November 2011)

essential social infrastructure with attention to the needs of poor communities; to support women to contribute and benefit from development; to improve the poor's access to and engagement in governance processes; to remove barriers to the participation of the poor including in decision making; to assist in developing more effective, efficient and transparent administration; and to support actions that take account of disadvantaged groups including minority groups, people with disability and the aged.

Gol has issued a *Presidential Decree No.15 2010 on the Acceleration of Poverty Reduction* which emphasises engaging with poor and vulnerable groups; improving the quality and quantity of policy alternatives for poverty reduction; and enhancing the effectiveness of poverty reduction measures.

As poverty reduction is a priority for both GoA and Gol, improved sanitation and solid waste management is a critical issue which the sAIIG will help to address in participating cities. While the program will not focus solely on poor households, poor members of the community will benefit from its implementation. Ensuring that appropriate measures are taken to include the poor and other disadvantaged groups is of concern for this design and further details can be found in Annexe 7 and the PMM.

#### **4.9.1 Gender equality**

Gender equality in development is of interest for both GoA and Gol. GoA policy requires that gender equality is taken into account in all development activities, while Gol *Presidential Instruction (INPRES) No.9/2000* and the Medium Term National Development Plan 2010-2014 (*Rencana Pembangunan Jangka Menengah Nasional 2010-2014*) require that gender is mainstreamed for more effective and equitable development. The IndII gender strategy and plan provide strategic direction and actions for improved gender equality which are required to be integrated into IndII- supported activities. Details of the gender inclusive approach for sAIIG can be found in Annexe 7 and the PMM.

The sAIIG's effectiveness, efficiency and sustainability will be increased by ensuring that a gender inclusive approach is adopted and that women's rights are considered. Socialisation and information dissemination will be designed to reach both women and men so that there will be equitable participation by women and men within the household in deciding to connect to the sewer service provided by the sAIIG.

The sAIIG design includes three mechanisms to encourage implementation of the proposed social and gender inclusive approaches:

- (a) Consultants will provide gender awareness input to LGs to apply gender and socially inclusive approaches for their interaction with the community in implementing sAIIG activities. This will include guidance to LGs for development of awareness-raising and social marketing strategies to reach women and men from all socio-economic levels.
- (b) The Baseline and Verification Consultants will collect qualitative data at community and LG levels. Quantitative questions related to household access and participation will be included in the socio-economic surveys to assess levels of overall participation and the participation of women and the poor in project design and implementation.
- (c) IndII carries out routine gender case study evaluations across all its activities; selected sAIIG activities will be subject to such evaluations.

#### **4.9.2 Disability**

Disability is a core concern for AusAID. AusAID's disability policy has a number of expected outcomes. The policy outcome particularly relevant to the implementation of the sAIG activity is for improved quality of life for people with disability through disability inclusive development. Other especially relevant aspects of the policy are to ensure access to infrastructure for people with disability and the need to model good practice with regard to disability inclusive development. Guiding principles include the need to promote and enable active participation by people with disability and to recognise that people with disability hold the same rights as others.

#### **4.9.3 Child protection**

AusAID's child protection policy, applied in all aid delivery, requires zero tolerance by AusAID personnel and contractors of any form of child abuse, including child pornography. The general issue of child protection is considered in IndII's risk management strategy which is applied to all activities.

#### **4.9.4 Anticorruption**

In line with its aim of supporting Indonesia's efforts to reduce corruption, the sAIG program will adhere to the three main pillars of the 2004–2009 RAN-PK<sup>29</sup>: (i) prevention; (ii) enforcement; and (iii) monitoring and evaluation. Implementation of the program will also be guided by Australia's anti-corruption approach of: (i) building constituencies for anti-corruption reform; (ii) reducing opportunities for corruption; and (iii) changing incentives for corrupt behaviour.

sAIG will follow an output-based methodology such that grant funds are only disbursed after works have been completed, are in operation, and have been verified by an independent consultant. This output-based methodology and the fixed cost menu used for sAIG allow the levels of corruption risk to be considered sufficiently low that a program-specific Anti-Corruption Action Plan is not required. In addition the grant agreements will include a mechanism for recovery of funds from the LGs should evidence of ineligible expenditure be found after the grant has been disbursed.

To promote the principles of transparency and accountability LGs will be required to establish a sAIG specific web-site, or feature prominently sAIG content on their own web-site, for public disclosure of the details of all procurement and contract awards, which they will update within one week of contract awards.

MoF and the CPMU will use the computerised financial management system developed with the World Bank for the Local Government & Decentralisation Project (DAK Reimbursement) in 2010 to improve accountability. This system aims to make the project financial information and outputs transparent to all internal stakeholders: MoF, BAPPENAS, MPW, IndII, and LGs. Access to the system will be controlled by MoF, which developed it with MPW; the system is linked into MPW's MIS. MoF will be responsible for uploading data on sAIG grant allocations and transfers, while the LGs will upload data on local budget allocations and contract awards.

Information on sAIG outputs collected by IndII consultants will include: project location, GPS coordinates, technical data, physical progress and photographs of the sub-projects. The CPMU will upload verification results of completed sub-projects.

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<sup>29</sup> Refer: Australia Indonesia Partnership - Anti-corruption for development plan 2008–13, p. 4

In addition, the AusAID “Anti-corruption for Development Plan” will be socialised with officers and stakeholders responsible for managing all aspects of the sAIG program, including: MoF, MPW, and LG officials.

#### **4.10 Compliance with the *Environment Protection and Biodiversity Conservation Act***

*The Commonwealth of Australia Environment Protection and Biodiversity Conservation Act 1999 (EPBC Act)* is the legislative basis for environmental protection and management in Australia under which IndII is legally obliged to ensure appropriate measures of environmental compliance and protection are incorporated into all the facility activities, including the sAIG. The *EPBC Act* came into effect on 16 July 2000, and is Australia’s principal national legislation for the protection of the environment for activities supported by AusAID worldwide. As a facility, IndII must comply with GoA and Gol environmental protection legislation and related multilateral agreements signed by Australia and Indonesia. Gol has a number of legislations that provide for environmental management and protection applicable to sAIG (see Annexe 8).

##### **4.10.1 PPSP sAIG and the environment**

The sAIG supports the Indonesian nationwide initiative to accelerate the development of sanitation services (Percepatkan Pembangunan Sanitasi Permukiman, PPSP) in 330 cities to support the nation's commitment to meet the Millennium Development Goals (MDG) for water and sanitation by 2015.<sup>30</sup> MDG Goal 7: Ensure Environmental Sustainability, is the overarching goal for this initiative (see Annexe 8). Both GoA and Gol recognise that the environment is a comprehensive system comprising biophysical, built, economic, and social/cultural aspects, making it a cross-cutting issue for all development activities. Implementation of PPSP is intended to take place over six stages. LGs wishing to join sAIG should be at PPSP Stage 4, which seeks to establish a sector memorandum of understanding (MOU) based on the sanitation strategies developed by the districts/cities, see Annexe 8. The sector MOUs should consolidate the PPSP strategy and be elaborated in the district/city plans.

##### **4.10.2 IndII environmental management and sAIG**

The AusAID Environmental Management System (EMS) forms part of the IndII Environmental Compliance and Environmental Management Process (ECOMAP) which incorporates GoA and Gol environmental screening and measures (see Annexe 8). As the PPSP is a sector wide initiative with direct implications for district/city plans as noted above, *Act No. 32/2009 on Environmental Protection and Management* requires that a strategic environmental assessment (SEA) be undertaken to exercise environmental due diligence and ensure compliance of these plans with environmental standards and safeguards. It is highly likely that some PPSP activities will be subject to a SEA. Consultation with the Environment Ministry will confirm the format and level of detail for such an assessment. Although PPSP activities may be subject to a SEA, sAIG is designed as a series of independent, small-scale initiatives with the potential to cause short-term, local negative environmental and social impacts. In most cases mitigation measures can be designed more readily for projects at this level. Individual design specifications and the proximity of these facilities to sensitive areas of biodiversity, or identifiable

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<sup>30</sup> United Nations Development Group (2003), Indicators for Monitoring the Millennium Development Goals - Definitions Rationale Concepts and Sources; United Nations Development Group - United Nations Population Fund, United Nations Development Programme, and the Department of Economic and Social Affairs–Statistics Division

impacts contributing to climate change, will dictate whether the sub-project at a specified location requires a full EIA.

#### **4.11 Critical risks and risk management strategies**

As a new program, sAIIG will be subject to risks, however the use of the output based modality will significantly reduce risks on the application and delivery of the grant. The risks identified are summarised in the Summary Risk Matrix on the next page; the detailed risk identification, management and mitigation proposals are given in Annexe 10.

The full extent of the risk profile for the proposed program will be better known as the implementation of the Phase I IEG activity progresses through 2011 and the lessons learnt are realised and documented. There are indications at this stage of some risks in the use of the IEG funds. Adequate safeguards are in place to detect the misuse of grant funds and intervene, but such intervention increases the possibility of non-disbursement of the allocated funds. Many of the identified risks are related to procurement and implementation aspects under the current modality. The shift to output-based delivery of the grants will reduce the procurement risks but not eliminate them. Construction quality will also remain an issue. For those reasons procurement quality will be one of the key governance milestones in the grant agreements and a central requirement for LGs to retain the grant awards. Construction quality will be addressed through dedicated field supervision and periodic review, prior to the handover of completed works, by independent consultants engaged under IndII contract. Post procurement audits will be carried out periodically by the independent review consultant. The relevant ministries will be fully engaged in conducting the audits, in order to meet the program's governance objectives.

Additional monitoring and oversight will be achieved through a publicly accessible web site promulgating the program and the award of grants to LGs. Such websites have served as effective tools for good governance in PNPM, Pamsimas, and other projects. LGs will be required to establish sAIIG specific websites or feature prominently sAIIG content in their own websites to disseminate at a minimum, status of implementation, tenders, and results of procurement.

The option of multi-year implementation will allow adjustments to grant allocations among LGs based on annual reviews of performance. Each LG will also be able to adjust its use of the grant from year to year to make up any applications not approved for reasons of non-compliance with standards or quality. These options will greatly reduce the risk of non-disbursement of the grant and allow flexibility for LG to adjust to annual variations in budget resources.

Under this modality, both GoI and IndII will have significant prior experience with the application of the Water Hibah, Sanitation Hibah and IEGs to adequately identify and manage risks associated with the sAIIG program.

The sAIIG model and modality does not threaten any stakeholder interests, rather it is highly complementary to the current policy environment and is strongly endorsed by DGHS, MoF and Bappenas.

DGHS has committed considerable resources to implementing the IEG as well as the Water and Sanitation Hibah. DGHS see the IEG program as a strong tool to encourage better governance in the sector under a decentralised environment. Indications to date are that DGHS will continue to commit resources for the implementation of the sAIIG.



## SUMMARY RISK MATRIX

Risk	Impacts	Risk Rating	Mitigation Strategies
Instigating new program	<ul style="list-style-type: none"> <li>• Unclear roles and responsibilities</li> <li>• Insufficient program management</li> <li>• Capacity/commitment of Partner Agencies</li> </ul>	High	<ul style="list-style-type: none"> <li>• Agreement on AusAID/IndII/Partners roles and responsibilities</li> <li>• DGHS committed and processes in place from previous Hibahs</li> <li>• Program management plan and related processes implemented</li> </ul>
Program governance	<ul style="list-style-type: none"> <li>• Loss of focus</li> <li>• Insufficient management control and direction</li> </ul>	Medium	<ul style="list-style-type: none"> <li>• Agreed program management monitoring and reporting</li> <li>• Regular communication with stakeholders</li> <li>• Implementation of governance board</li> </ul>
Grants management	<ul style="list-style-type: none"> <li>• Processes and procedures unclear</li> <li>• Contract disputes</li> <li>• Grant payments deferred</li> </ul>	High	<ul style="list-style-type: none"> <li>• Grants management process clearly defined and documented</li> <li>• Required outputs clearly defined and documented</li> <li>• Payment processes clearly defined and documented</li> </ul>
Lack of overall LG Governance	<ul style="list-style-type: none"> <li>• Embedded risks <ul style="list-style-type: none"> <li>○ Poor procurement</li> <li>○ Contract disputes</li> </ul> </li> <li>• Grant payments deferred</li> </ul>	High	<ul style="list-style-type: none"> <li>• Improved LG governance – program objective</li> <li>• Required outputs and LG role clearly defined and documented</li> <li>• Baseline and verification requirements and processes clearly defined and documented with LG</li> </ul>
Limited capacity of LGs for pre-financing	<ul style="list-style-type: none"> <li>• Program unable to deliver outcomes</li> <li>• Slow uptake</li> <li>• Payment of grants deferred</li> </ul>	Medium	<ul style="list-style-type: none"> <li>• Clearly defined grant agreements</li> <li>• Menu of items and associated costs clearly articulated</li> <li>• Support from DGHS and MoF</li> <li>• Selection criteria includes funding ability</li> </ul>
Financial risks	<ul style="list-style-type: none"> <li>• Fraud</li> <li>• Corruption</li> <li>• Payment disputes</li> </ul>	Low	<ul style="list-style-type: none"> <li>• Output-based modality transfers risks to LGs</li> <li>• Grant management process clearly defined and documented</li> <li>• Verification process defined and documented</li> </ul>