

Updated Project Information Document (PID)

Report No: AB894

Project Name	ISLAMIC REPUBLIC OF IRAN - IR-Urban Upgrading and Housing Reform
Region	Middle East and North Africa Region
Sector	Housing construction (40%); Central government administration (20%); Housing finance and real estate markets (20%); Roads and highways (10%); General water, sanitation and flood protection sector (10%)
Theme	Personal and property rights (P); Access to urban services for the poor (P); Municipal governance and institution building (S); Participation and civic engagement (S); Gender (S)
Project	P073433
Borrower(s)	ISLAMIC REPUBLIC OF IRAN
Implementing Agency(ies)	MINISTRY OF HOUSING AND URBAN DEVELOPMENT (MHUD) Address: Contact Person: Dr. Ali Abdolali-Zadeh, Minister of Housing and Urban Development Tel: Fax: 98-21-877-6711 Email:
Environment Category	B (Partial Assessment)
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1. Country and Sector Background

The 3rd Five Year Development Plan (1999/0-2003/4) gave a prominent role to the housing sector and the 3rd Housing Development Plan set out four strategic objectives that aim at (i) increasing the flow of long term domestic and foreign resources for housing finance in tandem with the adoption of adequate building technologies and the development of a professional and efficient construction industry, (ii) promoting financing for and mass production of small housing units adapted to the needs and affordability of low-income and vulnerable households, (iii) improving the efficiency of taxation and subsidies in the housing sector and to promote housing insurance, and (iv) reducing government controls and devolve responsibilities to local authorities (Provincial agencies and municipalities) for housing, urban land management (including government owned land) and promotion of rental housing and housing cooperatives.

While some progress has been achieved in the implementation of the 3rd Housing Development Plan, the Government will need to pursue and accelerate the reforms in several areas as outlined in the Bank Housing Sector Strategy Note of June 2002 and the ensuing Action Plan.

(a) Physical Infrastructure Constraints. During the last decade, Iran has experienced a rapid urban growth that has exceeded the capacity of the state and municipalities to extend urban infrastructure and services. It has resulted in a significant proliferation of under-serviced settlements. Many of these settlements are outside the official city limits and, therefore, not legally recognized by municipalities. Others are within the dilapidated historic center of cities that offer tremendous wealth of cultural heritage. Such settlements are estimated to constitute 20% – 30% of the urban fabric and are home to the poorest segments of the urban population.

(b) Natural Constraints. Iran is one of the most seismically active regions of the world. Earthquakes are considered to be the most destructive of all natural catastrophes that could happen in Iran. Destructive earthquakes occur regularly resulting in significant economic and human losses. Housing losses due to earthquake amount to an average of 1 percent of existing housing stock per year. The Iranian territory is frequently reminded of this by occurrences of disastrous earthquakes such as the most recent devastating Bam earthquake on December 26, 2003 ($M_s=6.3$).

(c) Demand Constraints.

Underdeveloped housing finance: Following the nationalization of the banking system in 1358 (1979), Iran has been operating for two decades under a financial policy of directed credit that includes a “specialized circuit” for housing finance. However, the supply of housing loans remains small (3% of GDP) when compared to Tunisia (6%) or Malaysia (22%). It is also below the objectives set by the current development plan for affordable housing. Presently, Bank Maskan (the Housing Bank), which is a specialized state-owned bank, is the dominant provider of long-term housing finance to households. Public commercial banks limit lending to shorter-term construction finance and savings mobilization proved to be difficult. Under pressure from the rapidly rising demand for housing, increasing numbers of subsidized or state-funded housing finance programs have been sponsored by several ministries or agencies and delivered by public banks to provide some relief to targeted social groups.

Inefficient system of housing subsidies: Preliminary estimates suggest that housing subsidies in Iran are significant and may reach 4.5% of GDP. Taking into account utility subsidies amounting to 3% of GDP, housing-related subsidies become excessive and may exceed annual housing investment (4.7% of GDP in 1996/7). These subsidies are: (i) mostly non-transparent and unaccounted for in any budget, (ii) inefficiently delivered, (iii) regressive in the form of interest rate and energy subsidies, and (iv) provided through a highly fragmented system. As such, their benefits accrue largely to households in higher income brackets. Furthermore, subsidies are granted to developers, financing institutions and buyers, leading to inefficiencies, speculation and deviation of subsidies from their intended beneficiaries. With very few exceptions, such as the Imam Khomeini Foundation, the intended population groups are not receiving the full benefits of government assistance. For many, such assistance is inaccessible.

(d) Supply Constraints.

Insufficient supply of undeveloped and serviced land. As urban land at the periphery of many cities is government owned, this leaves little room for the development of an active land market. The MHUD, which controls much of the public land, has initiated a new urban land development policy with the intention to increase the availability of developable land substantially. The focus of the ministry’s strategy concerning land management has been to provide infrastructure for new residential areas (including the development of new/satellite towns) and to supply developed land to individuals, construction companies and developers. Most of the land remains un-serviced and un-titled. Withholding such significant amounts of land stifles private sector contribution to urban development and seriously restricts the efficient operation of land markets.

Rigid Urban planning and management: Urban planning in Iran is directive and hierarchical in terms of both coverage and nature. The constraints created by the rigidity of urban plans and legal zoning have contributed to the proliferation of informal settlements in and around major cities. In response, the Government has started the rehabilitation of these under-serviced neighborhoods as part of a comprehensive review of current urban planning and management process.

(e) Institutional Constraints.

Lack of empowerment and engagement of local government: Although article 7 of the Constitution assigns major roles in the government structure to elected local councils, it was not until the 3rd Development Plan that appropriate actions to promote decentralization were given high priority. Decentralization has become the main thrust of the upcoming 4th development plan. A draft decentralization law that is expected to be enacted by the Parliament soon will reinforce the role of the city councils by transferring allocations of the corresponding budgetary resources and creating elected regional councils and inter-communal councils. Overall, it is envisaged that local authorities and other stakeholders will ultimately be empowered to make decisions on planning, budgeting, execution and management of city policy in response to the local needs and in line with national development plans and policy guidelines. This devolution of responsibilities will require, among other things, considerable training and institutional capacity building at the local level.

Fragmentation of policy decision-making and responsibilities: Numerous government institutions and organizations are involved in setting and implementing housing and urban policies and programs in Iran. The Ministry of Housing and Urban Development (MHUD) must deal not only with other central government bodies but also with the Housing Foundation, the Housing Bank and six affiliated organizations. This has resulted in multiple and disjointed housing programs, difficult development of a coherent and well coordinated housing sector policy. Consequently, housing markets in Iran are highly heterogeneous, precise knowledge of real housing needs is lacking (despite the wealth of housing information available) and access to subsidies has less to do with income than with location/ employment affiliation.

These constraints have resulted in: (i) a highly volatile private housing market; (ii) an unbalanced output in favor of large units; and (iii) a very fragmented financing through numerous small public housing programs.

2. Objectives

The key development objectives of the Project (APL1) are to (i) improve the living conditions in under-served neighborhoods in up to five provincial capital cities and; (ii) prepare the systems, capacity, and regulatory foundation and initiate market based housing sector reforms. To ensure that investments in upgrading are of high priority to their ultimate beneficiaries, municipalities are expected to undertake a strategic planning process with significant community participation.

3. Rationale for Bank's Involvement

The Bank has acquired international experience in supporting housing reforms and urban development. Throughout the MNA Region, the Bank has assisted borrowers on housing finance (Jordan, WBG, Algeria, Egypt) and slum upgrading (Morocco, Tunisia , Algeria, Jordan). In recent years, the Bank has been also renewing and strengthening its involvement in Iran through several on-going lending and grant operations in sectors such as banking regulation, sewerage, primary health care and local development. The proposed Project will build on the Bank international experience in housing reforms and incorporate lessons learnt from on going and passed lending operations in Iran.

4. Description

The Project objectives will be achieved through three main components: (i) urban upgrading and community enabling programs in up to 5 selected cities; (ii) technical assistance for housing sector reforms; and (iii) technical assistance and capacity building for Project implementation.

Component A – Urban Upgrading (US\$ 89.62 million)

This Component lays the foundation for launching a sustainable country-wide urban upgrading program through the implementation of the following sub-components:

A-1: Design and supervision of upgrading programs in APL1 cities.

A-2: Implementation of upgrading programs in APL1 cities:

A-3: Design of upgrading programs for APL2 cities

A-4: Design of financing arrangements for upgrading under APL2 and APL3

Component B – Housing Reforms (US\$ 3.0 million)

Component-B aims at enhancing housing affordability and efficiency of the housing sector in Iran in the long term. It will consist of foreign and local technical assistance, training and equipment for implementing the specific priority actions in reforming the housing sector as outlined in the Housing Sector Strategy and the ensuing Action Plan:

B-1: Housing and land management

B-2: Housing finance

B-3: Housing subsidies

B-4: Housing information

Component C – Project Management (US\$ 2.0 million)

This Component will finance: (i) the cost of office and ICT equipment required for Project management and implementation; and (ii) technical assistance for Project management and implementation, including hiring of individual consultants and consulting firms in areas of Project management, financial management and procurement, Project monitoring and evaluation including the documentation of the Project experience and study tours, training to key policy-makers and other.

5. Financing

Source (Total (US\$m))

BORROWER (\$20.00)

IBRD (\$80.00)

Total Project Cost: \$100.00

6. Implementation

Project implementation is aligned with current institutional responsibilities in Iran and each Project component will be implemented by the relevant agency under the MHUD: Component-A – by the Urban Development and Rehabilitation Organization (UDRO), the main agency responsible for urban upgrading projects in historic cities; Component-B – by the National Land and Housing Organization (NLHO).

An Inter-ministerial Steering Committee (ISC) with representatives of the MOI, MEAF, the Central Bank (CBI), MPO, the High Commission for Architecture and Urban Development, and UDRO was established during Project preparation. Its main role is to provide guidance to the reform strategy and to the design of the Program. During the implementation, the ISC will be in charge of Program oversight. It will meet at least quarterly to review progress, coordinate decisions and remove impediments to the timely implementation of the Program.

7. Sustainability

The benefits of the Program are expected to be sustainable due to the strong emphasis on sequencing of reforms, capacity building and institutional development. There is also clear commitment by important stakeholders at the national and local government levels and considerable participation of communities in the design of the Project at all stages. The housing sector reform will reduce the budgetary burden of the government following the streamlining of housing subsidies (Annex 1b) and as the private sector plays a greater role in housing supply.

8. Lessons learned from past operations in the country/sector

(a) Piloting, phasing, and sequencing of reforms: While the objective of freeing up housing markets and devolving housing sector responsibilities to local governments and the private sector is clear, the Bank's experience shows that the means to realize this objective has to be carefully thought through in terms of building the necessary capacity, information systems, and the regulatory framework. In some cases such as subsidy instruments or land management, programs have to be piloted to test their effectiveness before they are scaled up. In others such as building codes, there is considerable local experience to allow for moving forward at the legislative level early on.

(b) Ensuring Readiness of the Borrower for Implementation: The common lesson in the past Bank-financed projects is that ensuring / building an adequate capacity for carrying out Bank Project specific activities such as procurement and disbursement are important. During Project preparation, intensive advisory support on the Bank's fiduciary procedures has been provided, the Bank will organize a seminar on procurement and disbursement during the Project's launch paying particular attention to the training needs of Project implementation teams at the local level.

(c) Early Involvement of Main Stakeholders: MOI, MPO, participating municipalities and CBI are the key stakeholders in municipal management, budget allocation and banking regulations. These stakeholders have been fully involved in the program preparation and are fully committed to the Project. The Project Team also consulted local communities in the under-serviced areas in the three pilot cities and initiated contacts with participating provincial governments and coordinated with them during Project preparation. The early participation of the stakeholders proved to be important for ensuring acceptance and commitment and securing availability of counterpart funds and indicating priority investments in urban upgrading.

(d) Sustainability of Upgrading Component: Projects that tend to focus on surgically upgrading a neighborhood in the absence of a citywide strategy and adequate capacity building are not likely to be sustainable as demonstrated by Bank's prior experience in other projects. Therefore, the Program focuses on training and capacity building of city officials and takes a citywide approach to upgrading.

(e) Ensuring Appropriate Procurement Environment in Iran: during implementation of other Bank Projects in Iran it emerged that Loan Agreements are often not fully understood and accepted by the concerned officials and precedence is usually given to the local rules, particularly, at the level of local governments. In addition, the Iranian authorities have restrictive rules in regards of contracting foreign consultants, suppliers and contractors, which is contrary to the Bank's recommended procedures. Country procurement issues, which may be in conflict with the Bank's recommended procedures, are presently being addressed by the Bank with the government in order to arrive at an acceptable solution to be applicable to all Bank projects in Iran.

9. Environment Aspects (including any public consultation)

Issues : The Project has been classified as Category B as per the Bank's Operational Policy 4.01 Annex C on Environmental Assessment, indicating that there are reversible environmental issues that can be mitigated. Due to the fact that the Project has a participatory approach and specific sub-projects will only be defined during the course of the Program, it is not possible to carry out environmental analysis ex-ante. The UUHRP is expected to bring significant environmental and health benefits and no major environmental issues are anticipated. A number of potential investment sub-projects have been received from the interested cities. A Bank consultant conducted a desk screening of these proposals and no irreversible impacts that could arise from these sub-projects were identified.

EMP for the Project was prepared in conjunction with the feasibility studies in Bandar-Abbas, Kermanshah and Zahedan and approved by the Bank. During the first year, environmental screening and assessment will be reviewed by the Project Team on a no-objection basis. During the second year, an evaluation of national capacities for approving environmental assessment will be carried out and a decision on the further set up will be taken. The environmental category and requirements for APL2 and 3 will be re-assessed during the appraisal of both subsequent phases.

10. List of factual technical documents:

- Environmental Management Plan
- Environment Guidelines Manual
- Resettlement Policy Framework
- National Strategy for Enabling Regularizing Informal Settlements
- National Housing Strategy

11. Contact Point:**Task Manager**

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Note: This is information on an evolving project. Certain components may not be necessarily included in the final project.