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THE REGULATORY ENVIRONMENT OF URBAN LAND IN INDONESIA:

CONSTRAINTS IMPOSED ON THE POOR
and
IMPACT OF WORLD BANK'S URBAN PROJECTS

By Alain Bertaud

Alain Bertaud has now retired from the World Bank and can be contacted at Duatreb@msn.com

THE REGULATORY ENVIRONMENT OF URBAN LAND IN INDONESIA: CONSTRAINTS IMPOSED ON THE POOR

"Typically [planning standards] are handed down as 'rule of thumb' from one situation to another, adapted by cumulated experience. Such norms are characteristically expressed as a simple inflexible per a given population, sometimes also including locational specifications. From the norms as usually expressed it is impossible to know the substantive justification - whether functional, economic, behavioral, social, psychological or environmental. Therefore, there is no easy way of modifying them to meet particular situations in a reasoned manner."

Hill and Alterman, "New Trends in Urban Planning". Pergamon, Oxford 1979, p.95.

Summary

i. Land development regulations have an important impact on the welfare of urban households even in a country like Indonesia where only about 20% of households live in regulations sanctioned housing. In Indonesia, poorly conceived regulations distort the land market, whether this market is formal or informal. The standards of primary infrastructure projects in the suburban areas are also distorted because regulatory densities are often used as projections. In reality, built densities are often 10 times the regulatory and projected ones.

ii. Most land regulations in Indonesia have a negative impact on poor households. They contribute to wastage of precious urban land, they require an unnecessary expansion of primary infrastructure, and they foster corruption.

iii. In the past, The World Bank has financed and is currently financing a large number of urban projects in Indonesia but has not addressed systematically the problem of the "quality" of regulations; it has concentrated mostly on improving processes. The successful implementation of two major Bank financed projects, KIP and BTN mortgages loans, requires a waiver of current land use regulations. However, the Bank has not yet addressed deliberately the need to improve the land development process through more adequate regulations. The first step would be to conduct an "audit" of current regulations and a cost benefit analysis for future regulations so that all households, even outside the perimeter of Bank financed projects, benefit from a more rational regulatory environment.

iv. The author proposes an agenda to improve the urban regulatory environment in Indonesia. This agenda, if implemented will benefit primarily Indonesian urban households by making land more affordable, but it will also improve the management of cities.

v. The data on income and distribution of the households correspond to all of Indonesia urban areas (cities above 20,000 people) . Serpong zoning case study is located in the South East of Jakarta periphery.

I. IMPACT OF LAND DEVELOPMENT REGULATIONS ON POVERTY

1. By shaping the rules under which the land and housing markets operate, land development regulations have a direct impact on the ability of the poor to have access to shelter. The welfare of poor households is largely dependent on their access to adequate housing. The location and characteristic of their dwelling would largely influence their chances of employment, their health status, and their children's opportunity for a good education. In Indonesia, like in many other countries, the social importance of shelter is well recognized, and with the intention of facilitating shelter access for the poor, the Government subsidizes mortgage interest rates. In addition, the Government subsidizes land development by financing the building of primary infrastructure from general revenues. The sub-

sidizing of interest rate and the financing of primary infrastructure gives the government major leverage in establishing and enforcing a series of regulations and planning practices, which influence in important ways how land and shelter markets operate and how municipal infrastructure benefits are distributed among the urban population. How those regulations and planning practices have an impact on the welfare of the poor is described below. The regulations have the effect of dividing the real estate markets into two independent markets, the formal and the informal. The benefits intended by the regulations are, (i) to lower the cost of land, and (ii) to provide "orderly" development allowing a more rational design and construction for primary infrastructure. I will show that none of these objectives is reached and that the cost of the regulations for households, for the government and for the economy of Indonesia is very high.

A. The Two Housing Markets

2. Trade and development of urban land takes place within two parallel markets: the formal market is heavily regulated and allows access to formal housing finance facilities with mostly subsidized interest rates, while the informal market operates under minimum regulatory constraints, but requires cash transactions or alternatively, is restricted to the informal finance system. This informal finance system is characterized by high market interest rates reflecting the constraints under which the market operates. One of the main constraints is the impossibility of using land as collateral. The 2 markets can be defined by a difference in tenure quality. Contrary to what happen in many developing countries the lower quality of land tenure of the informal market do not entail necessarily an insecurity of tenure, it only differentiates access to formal financing mechanism.

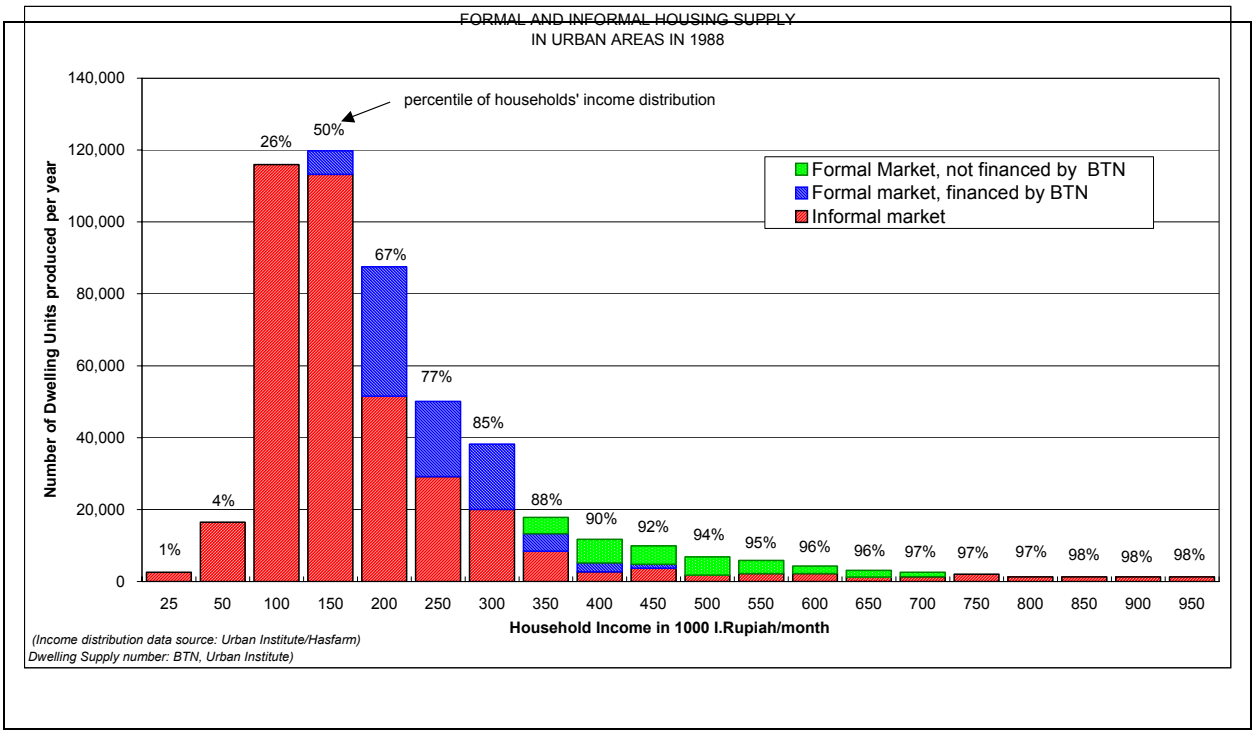
3. The formal market emerged only recently - in the mid-1970's - with the availability of Bank Tabungan Negara (BTN) mortgage financing, and is expanding rapidly. Both formal and informal markets are legal, but within the informal market various types of informal land titles are used, which provide different grades of tenure security, but preclude the use of land as collateral and hence, bar access to mortgage financing. About 20% of the dwelling units built annually are provided through the formal market. Those units are affordable to middle and high income households, while the range of units produced under the informal market covers all income groups. Most suppliers, whether they operate within the formal or informal market, compete for the same middle and high income clientele, although some specialized suppliers concentrate on the low income segment of the market exclusively within the informal system. Figure 1 shows the share in 1988 of all markets for new residential construction by income group. The large area of overlap by income group by the formal and informal market should be noted.

4. In Indonesia professional developers – who are the only suppliers of the formal market – must face a vast array of complex and costly land development regulations to develop land and build houses; individuals, by contrast, can trade land and build relatively freely. The land titles obtained by individuals have an informal character and provide a reasonable degree of tenure security. However, these titles prohibit the use of land as collateral thus precluding access to housing finance. Additionally, developers cannot use informal land titles to acquire and develop land and subdivide it later. Therefore, the development of tertiary and secondary infrastructure is impossible for households with informal titles. The present dual land development system has the advantage of providing easy access to land for many middle and middle-low income households. The disadvantage is that it slows down the development of infrastructure, making it difficult for small developers to enter the housing market, and restricting access to housing finance to a small group of households. The cumbersome regulatory framework applied to formal developers has several side effects: it fragment and distort land markets, and it pervert population density projections made for the planning and design of primary infra-structure and social services.

B. The Cost of the Formal Land Regulatory System

5. The use and transfer of urban land by formal developers are heavily regulated and, as a consequence, are costly and lengthy. The land development process takes an average of 32 months and the direct and formal costs associated with getting the necessary permissions have recently been evaluated at varying between 10% to about 30% of the cost of land /1. Land related regulations are taking many forms ranging from formal legislation to simple administrative practice /2. While government originally established each set of rules to provide a benefit to society, the original intent has often been forgotten. Current land law and regulations in Indonesia had never been the object of a periodic reevaluation to: (i) assess their relevance to present situation; (ii) measure their cumulative impact on land use efficiency; and (iii) monitor the financial burden they impose on low income groups.

FIGURE 1: FORMAL AND INFORMAL HOUSING SUPPLY



6. In Indonesia, the land subdivision legislation has three major objectives: (i) giving a legal tenure status to newly created plots; (ii) implementing urban development plans and physical planning policy; and (iii) coordinating the provision and extension of infrastructure /3. To meet those objectives, the land subdivision process requires the participation of numerous officials from various ministries and agencies assembled in committees, itself a costly process, but it would also normally require clear and realistic physical planning documents on which location decisions could be based. Because those documents do not always exist, or are not based on sufficiently accurate base maps,

/1 The legal system of land subdivision, its cost in financial terms and in time have been described and analyzed in a recent study prepared as part of the TA component of the Housing Sector Loan: "Land Titling for BTN Housing" by Michael Hoffman, Urban Institute/ Hasfarm, January 1989.

/2 The land development process requires three legal steps: (i) issuing of location permit; (ii) issuing of master Title; and (iii) splitting of Master Title. This process involve decisions by committees on a number of issues some legal other technical.

/3 Michael Hoffman, o.c...

location decisions are by necessity often arbitrary. In the major metropolitan areas for which detailed physical planning documents have been prepared, legal enforcement of plans are usually based on purely engineering or physical planning abstract considerations that results in a discriminatory effect on the poor (as discussed in more detail below).

7. In many developing countries the impact of the regulatory environment on urban development and poor households is often underestimated because land regulations are often openly broken and most development occur through a parallel informal system. However, the impact of legislation is not necessarily related to the number of people who comply with the law. The existence of a law creates a different flow of costs and benefits for households who comply with the law and for those who break it. A large number of individuals choose to forego the benefits associated with the law to avoid paying its costs, but this it does not necessarily imply that the law has no impact. For instance, to have access to housing finance, households have to buy a housing unit in a settlement which has been formally developed, i.e., a settlement for which a developer proceeded through three legal phases required under Indonesian law: 1) obtaining a location permit; 2) releasing of rights; and 3) granting of rights. However, only about 20% /4 of dwelling units supplied yearly on the housing market are provided through formal sector schemes that follow legal land development procedures. Therefore, about 80% of households are de facto unable to benefit from housing finance facilities. The impacts of the land development regulatory system on the whole population are important in spite of the fact that only a minority of households live in settlements which have been developed according to the land development legislation.

8. The land regulatory environment has a negative effect on the poor for two reasons: (i) the cost to comply with the law is often unaffordable to poor households; and (ii) many regulatory practices create distortions in the land market and in the distribution of urban services. Those distortions greatly increase the cost of urban development and shelter. When drafting a new land regulation, there is often an exclusive focus on the assumed social benefits that the law will provide, but the cost and distortions associated with it are often ignored. The cumulative effect of zoning regulations, maximum densities, minimum standards, etc., on poor households is almost never evaluated. Costs associated with land regulation include: (i) the cost incurred by the government in administering and enforcing the regulations; and (ii) the cost to households and enterprises to comply with the standards set by those regulations.

C. The Costs of Land Regulations: Costs to Government

9. In most cases, governments establish a regulatory process without evaluating the recurrent administrative costs implied. Typically, the institution assigned to administer and enforce the regulations does not receive the necessary resources required to enforce the law in an efficient manner. Hence, long delays occur in delivering titles, permits, and authorizations to those households willing to comply with the law. Confronted with long and costly delays, many developers and households make informal payments to government officials to expedite the process, substituting their own resources to finance part of the government operating costs. We should consider this type of corruption as an management problem rather than as an ethical problem. Changing the way building permits are given might be a more effective way to reduce government corruption than to try to make enquiries and use the judiciary system. Developers make informal payments because of the government's failure to match the complexity of regulatory instruments with the appropriate level of "operation and maintenance" resources. The process, which consists in making informal payments to obtain in a shorter time what the law authorized, is inefficient, and discriminates against the poor. It is an inequitable way of paying the equivalent of a user fee. The "bribe for process" system is inefficient because a surge in the number of requests for building permits would cause longer delays in processing and, as a consequence, would cause higher informal payments. However, those higher costs to developers and households would have no direct effect on the allocation of resources by the government to hire more clerks to accelerate the delivery process. Therefore, a surge of requests for building permits would simultaneously increase both the cost and the time required to obtain those permits. The cost of shelter would increase in a regressive manner as informal payments often represent a larger percentage of the shelter cost for low cost housing than for more expensive types of housing. For instance, in the last five years in Jawa Barat Province, the average time for issuing land rights in subdivisions has risen from 17 to 28

/4 "Constraints on the Supply of BTN Financed Housing by Private developers in Indonesia" Roy Gilbert, Michael Larkin, Urban Institute/Hasfarm, January 1989.

months /5. This increased delay is strongly correlated with an increased development activity. Although no data exists on the informal payments that are required from those who want titles in a shorter time, the assumption is that the costs would have risen together with the delays.

D. The Costs of Land Regulations: Costs to Households

10. The costs of land regulations to households are of three types:

(a)Direct costs to meet minimum standards;

(b)Costs in time and manpower to obtain necessary titles and permits, plus informal payment costs to substitute direct payment to government operation and maintenance cost; and

(c)Informal payment costs occurring when laws are imprecise and lack a clear purpose i.e. when money has to be paid to change a decision rather than to accelerate it.

11. The direct costs of meeting minimum standards are of course falling mostly on the poor. For instance, the regulating of minimum plot size increases the costs to households who would have normally opted for a smaller plot size than the one mandated by the law. In Jakarta area, the minimum legal standards for a dwelling unit result in a minimum cost of about Rp 4 million per unit. By fixing minimum standards, the law establishes implicitly a de facto "minimum standard income". If households fall below this "minimum standard income" they would have to obtain shelter through the informal sector. It is true that in Indonesia households belonging to the informal sector are well tolerated and are running few tenure security risks. However, by being unable to afford the minimum shelter consumption standards imposed by the legislation, these low income households forego a number of benefits that are reserved to the formal sector. In this way, poor households are made to pay either a direct cost if they decide to meet minimum standards and therefore pay more for shelter, or an indirect cost if they cannot afford the minimum standards and as a consequence loose the benefits of belonging to the formal sector.

12. The present system disadvantage small entrepreneurs when they need to obtain a title or building permit. Large developers are using full time "file pushers" to quicken the pace of processing. Small entrepreneurs and households lack the resources and know-how to do the same things. The additional time and cost involved in getting the legal permits is so costly that they often prefer to relinquish the benefits attached to the formal process, particularly access to housing finance.

13. Additional types of informal payments become unavoidable when the objectives and definition of regulations are so imprecise that the granting of a permit rests entirely on the arbitrary judgement of a civil servant. For instance, a private developer intending to develop a piece of land has to seek, first, a "location permit", and, in a second stage, a "land rights grant". The two different committees, from which those permits and grants are requested, will have to decide whether the proposed use is consistent with Government policy and is in conformity with current land use plans. In most cities of Indonesia, the government spatial planning policy is vaguely formulated and is subject to interpretation. In others, like Jakarta for instance, detailed land use plans exist but the limits between zones and the maximum densities imposed are themselves arbitrary and their ultimate purpose unclear. Because the law is often imprecise or appears arbitrary and surveying tools and detailed topographical maps are not always available, the final decision concerning what can be built in which location is left to the discretion of the civil servant who is in charged of enforcing the law. In fact, the legislation acts as a form of partial transfer of property rights from the landowner to the government employee in charge of enforcing land use laws. It is not surprising to see the government employee selling back this partial right to the original owner under the form of a permit.

/5 Michael Hoffman, o.c. p.73. The issuing of land right is only part of the titling process, the total time required for the approval of a land development scheme is in the range of 2.5 to 3 years.

E. The Boundary Between the Formal and Informal Sector is Set by the Cumulative Effect of the Costs of Land Regulations

14. The costs of meeting minimum standards and processing titles and permits, constitute a threshold below which land cannot be developed legally. Households who can afford and are willing to pay for a dwelling above the threshold price become part of the formal sector, the others become part of the informal sector. The ratio between formal and informal shelter sector is entirely determined by the cumulative cost of land regulations. A reduction of the minimum plot size by 10 square meters would immediately increase the number of households in the formal sector and the number of households with access to formal housing finance. In Indonesia, the major cost associated with the formal sector is not the costs of minimum physical development standards per se, but the costs incurred on account of the complexity of the administrative land subdivision system.

15. The most important benefits attached to the formal sector are not derived directly from the law itself, but are derived indirectly from complying with the law. For instance, the major benefit of possessing a formal land title is not the security of tenure that this title guaranties, /6 but the access to housing finance allowed by the title. The other potential benefits of formality is supposed to come from the "orderly development" resulting from following zoning and master plans. However, most of the direct benefits of urban planning laws and regulations are difficult to evaluate, we will see with the example below that often these benefits might well be negative. The spontaneous order generated by market forces appears as chaos to urban planners and municipal engineers unfamiliar with land market mechanisms. Most of urban laws and regulations are being created to introduce a recognizable geometric order in an apparently amorphous and random urban development growth. The geometric order attempted but never achieved through "development control" legislation is often naive. Its effect is mostly to distort market signals and to promote utopian development standards (see below Serpong example).

16. Informal sector and poverty are not synonymous. The poor are at the lower end of the income scale in the informal sector, but a number of middle-income households may choose the informal sector through economic reasoning and for the reasons explained above.

F. Zoning Regulations are Distorting Land Markets: The case of Serpong

17. Zoning regulations are formulated through maps which delineate areas where the type of land use and physical standards are restricted to those authorized. While in Indonesia zoning maps themselves have no legal status, they have a de facto legal status, because they are used as references by the committees examining the merits of developers requests for land development. Through the decisions of the committees, the zoning maps and regulations acquire a legal status that Indonesian lawmakers did not originally envisage. Indeed, the obligation of the committees is to guide and enforce through its decisions the spatial development policy of the Government. This is one of the stated objectives of the Indonesian land subdivision legislation.

18. Because they are used to buttress the decision to grant building permits, the zoning maps have an important impact on the supply and location of new housing built by formal developers. The areas in the urban fringes covered by zoning maps increase every year. The impact of zoning regulations on the supply of housing will increase in the future and therefore it is important to review the objectives and the methods used in the preparation of the maps. The technical criteria used for the design of the zoning plans are unclear. The objective of zoning is often defined as providing "orderly" or "rational" development. The conceptual ideas which guide the design of zoning maps are extremely abstract and outdated. They could be summarized as follows:

(a)Separation of functions into homogeneous zones;

(b)Allocation of space according to future "needs" calculated based on projected population increases and

/6 In case of expropriation, for a similar property, a larger compensation will be paid to the holder of a formal title than to the holder of an informal one.

densities;

(c)Creation of large land reserves for non identified future government use where development is forbidden;

(d)Design of a primary infrastructure network serving the area zoned that is based on perceived "needs" with no regard for compatibility with local and national budget; this include of course land reserve for an often extravagant number of highways or very wide roads

(e)Disregard for existing settlements, existing development trends and existing infrastructure; and

(f)"Cost is no object" approach to land development.

19. I will use the case of the master plan of Serpong to illustrate quantitatively the points made above. Serpong is a small town in the South East of Jakarta Metropolitan Area where development pressure is already high. In itself making a development plan is not a bad idea. But in this case the plan is so restrictive and have standards so different from the current standards used in Jakarta that the effects can be only negative. In restricting the use of land, zoning regulations are reducing the amount of land on the formal market. The zoning plan of Serpong (Figure 2. and 3.) restricts residential use to only 34% of the total land area /7. By artificially reducing the supply of land, zoning regulations increase the price of land. The areas zoned as residential, i.e. where formal development is allowed, do not necessarily coincide with land which is ready for development or where developers feel that residential demand exists. As a consequence, the supply of land for formal development is limited to the areas that are common to approved residential zones and where actual demand exists. In Serpong, for instance, a large part of the area zoned residential has no direct road access and will rely on infrastructure built in the future for that access. As no developer can risk acquiring land in areas without access, the area of developable land that is in fact on the market is further reduced. The area that is both directly accessible and authorized for housing by the zoning plan is only about 15% of the total land area.

/7 This restriction is in contradiction with the regional policy in Jabotabek area which tries to encourage urban growth along an East-West axis as opposed to the present North-South axis. According to Jabotabek master plan, Serpong is Class III area where growth should be encouraged, it is also immediately adjacent to Tangerang which is the fastest developing area in Jabotabek.

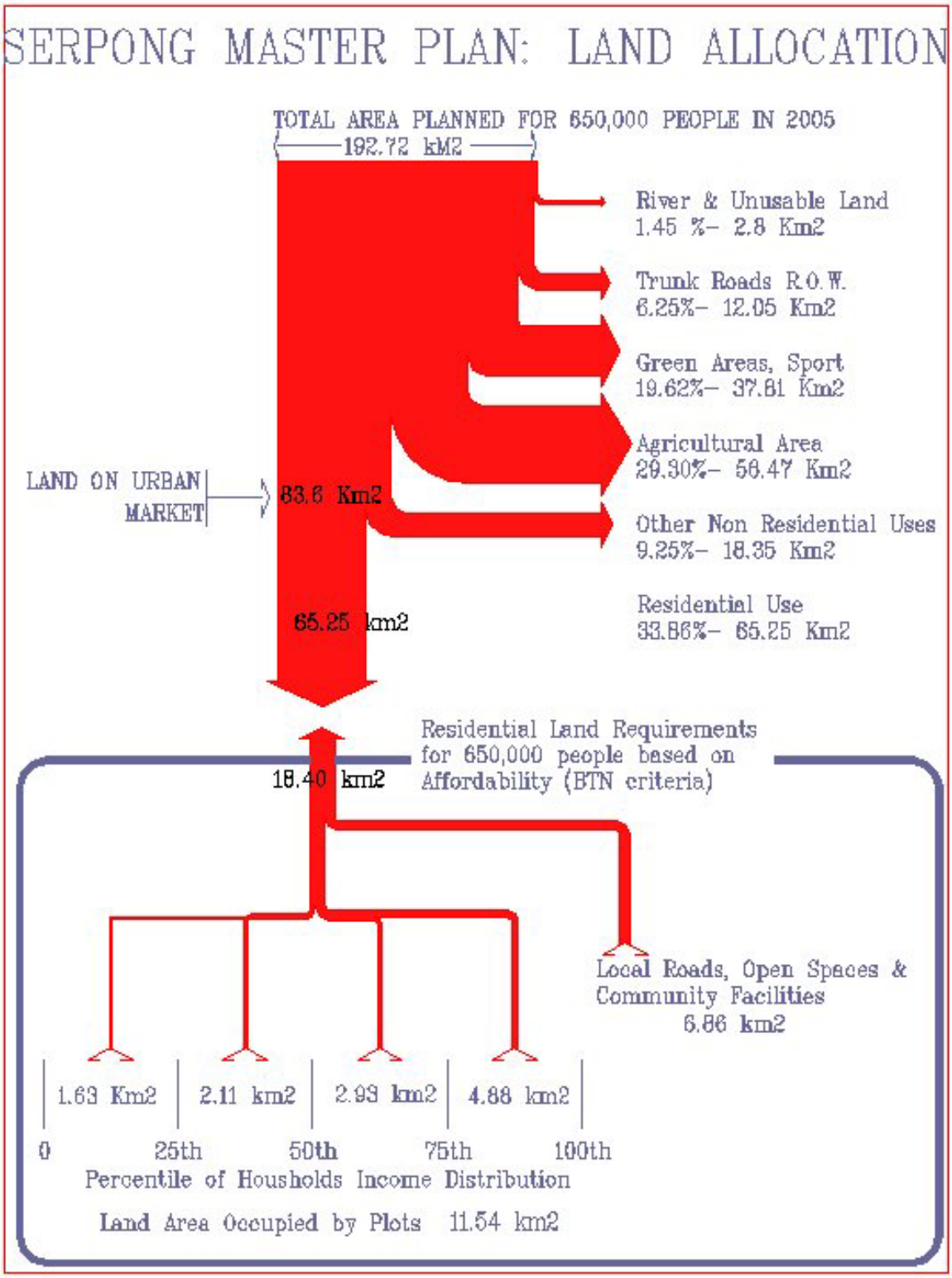
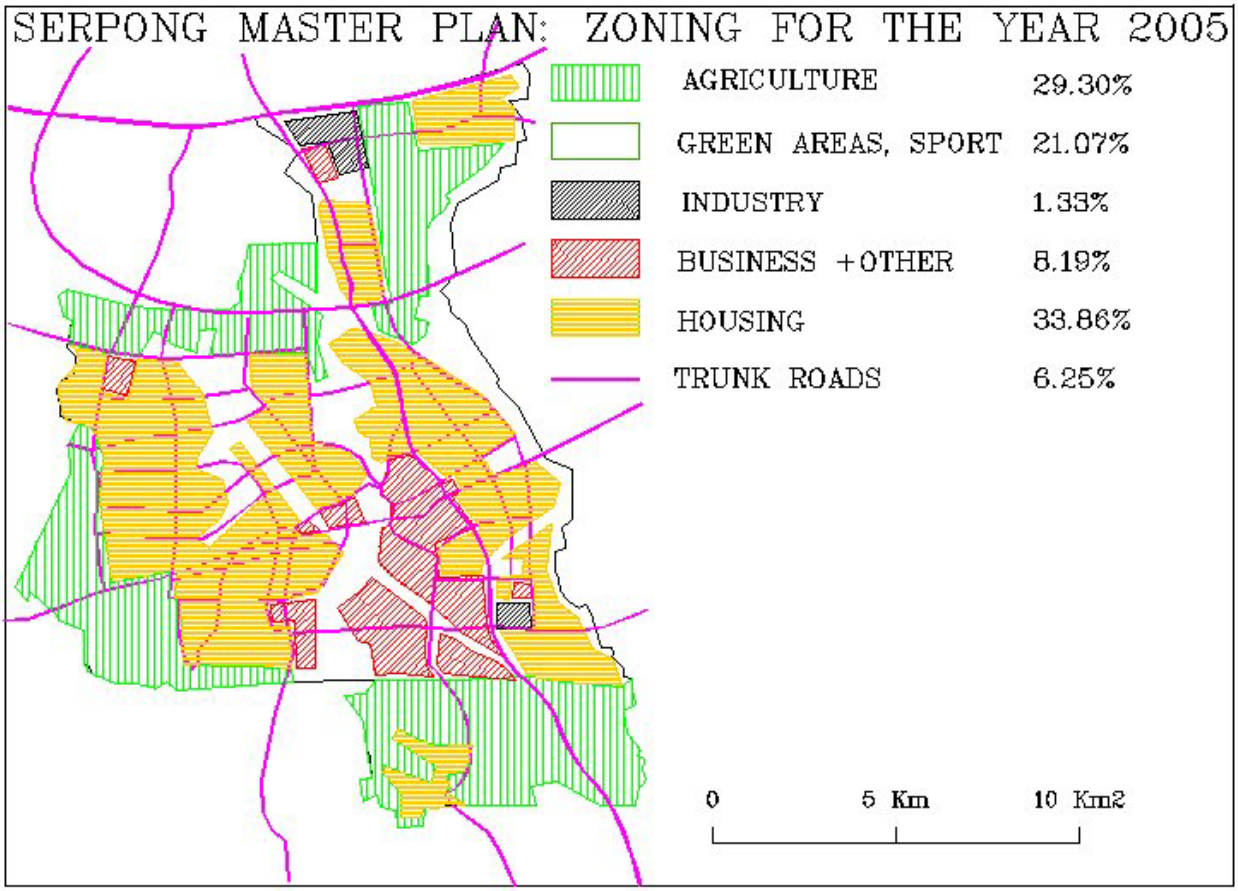


FIGURE 2: SERPONG MASTER PLAN - LAND ALLOCATION

FIGURE 3: SERPONG MASTER PLAN - ZONING FOR THE YEAR 2000



20. In addition to land use restrictions, zoning regulations impose a control on population densities. Planned densities are usually much lower than the actual densities in middle income residential developments. For instance planned densities in residential areas in Serpong have an average of 56 persons per hectare. By contrast, densities in middle income developments of the type financed by BTN vary from 300 to 500 persons per hectare, which correspond to plot sizes ranging from 60 to 90 square meters. The amount of land per household that corresponds to the permissible density is about 830 square meters, this would produce an average plot size of 500 square meters, which would be affordable by only about 5% of the urban population in Jakarta metropolitan area.

G. Zoning and Density Regulations are Distorting the Planning and Supply of Infrastructure

21. The primary objective of master plans is not only to "control" development through zoning regulations, but also to provide municipal line agencies with a medium and long range forecast of the spatial distribution of population and economic activities. Line agencies are supposed to coordinate their capital investment plan with the help of master plan projections. One of the major conceptual flaws of traditional Master Plan methodology is that land use zones and prescribed densities are transformed from prescriptions into projections, or in other words from what should be - in the opinion of the planner - into what will be. This confusion between regulations and reality has particularly grave consequences for the poor. As discussed above, the poor cannot afford the minimum standards prescribed by the regulations. The poor therefore will obtain housing only through the informal housing supply, mostly by increasing densities in existing villages. The standards used by poor households in the informal sector are the ones that are affordable under the conditions imposed by the combined effects of regulatory distortions and the limited urban services available.

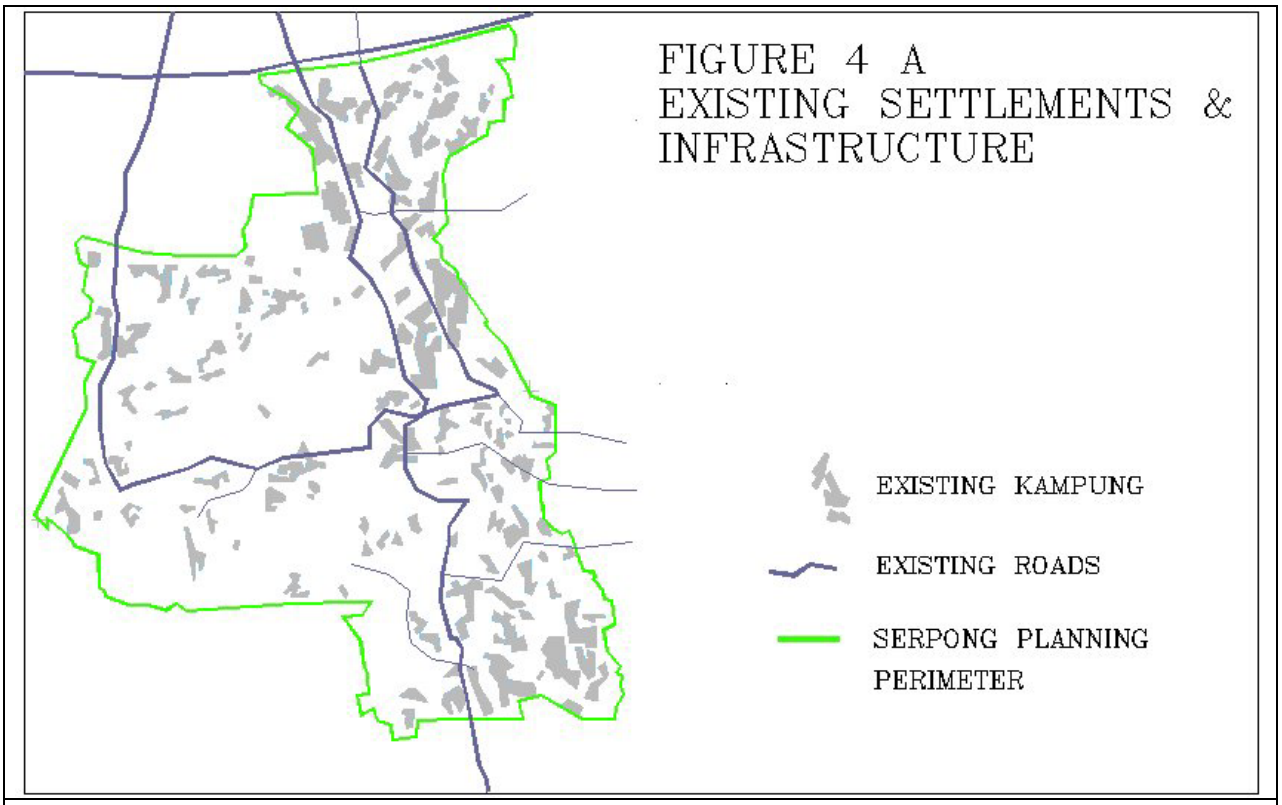


FIGURE 4 A
EXISTING SETTLEMENTS & INFRASTRUCTURE
EXISTING KAMPUNG
EXISTING ROADS
SERPONG PLANNING PERIMETER

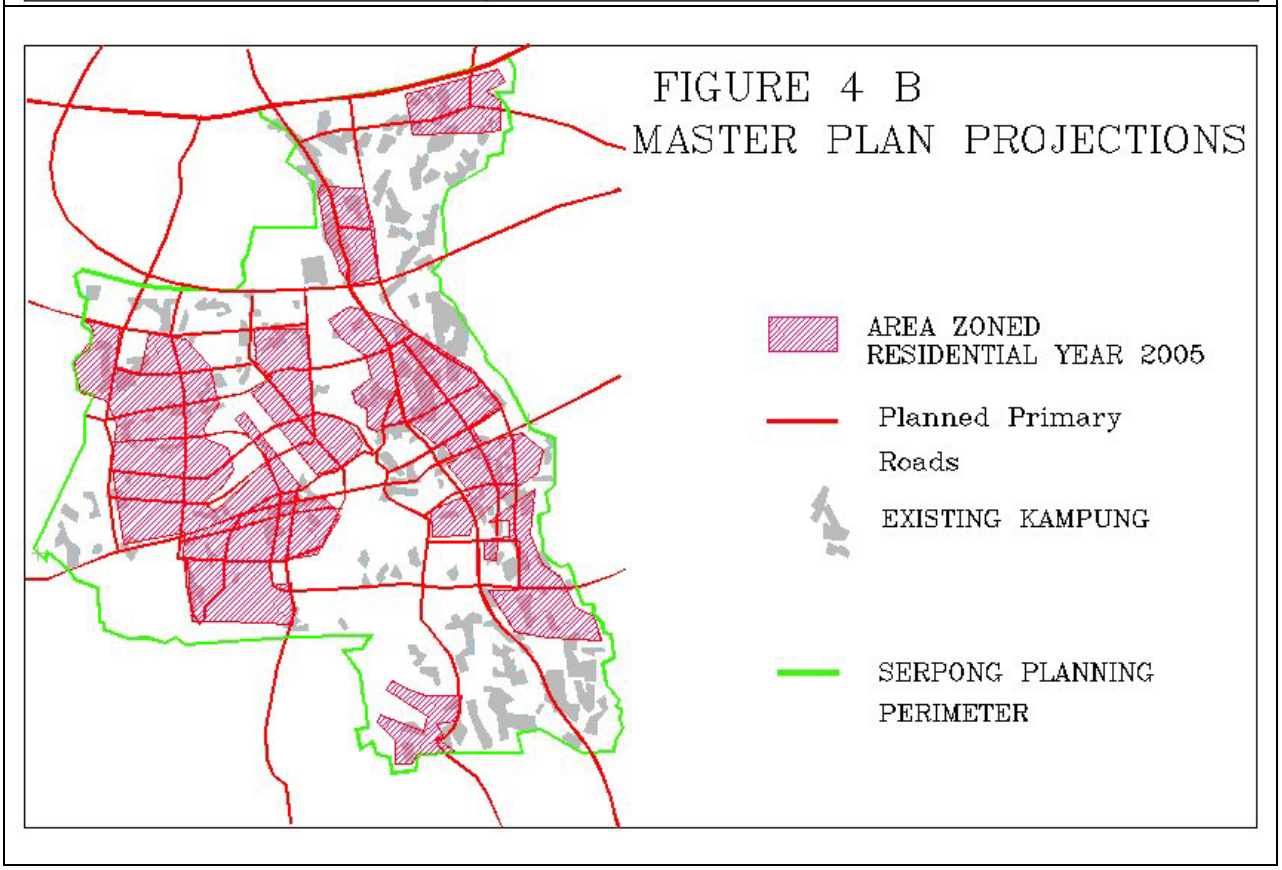


FIGURE 4 B
MASTER PLAN PROJECTIONS
AREA ZONED RESIDENTIAL YEAR 2005
Planned Primary Roads
EXISTING KAMPUNG
SERPONG PLANNING PERIMETER

22. Master plans, by confusing the unavoidable reality with the regulatory fiction, are misleading the line agencies into planning and providing infrastructure and services for a population whose future geographical distribution will be directed by regulations rather than by predictable economic constraints. The master plan of Serpong illustrates this point: Figure 4-A shows the existing road networks and the area occupied by villages. The population of the villages shown on Figure 4-A had been estimated at about 160,000 people in 1985, not an insignificant figure!. Figure 4-B shows the projected residential areas and the planned road infrastructure network. It can be seen that:

(a)Most of the villages are outside the areas zoned as residential; and

(b)The new road network /8 is designed to cater to formal residential areas planned at densities unaffordable to the poor or even to the middle class urban population.

FIGURE 4: SERPONG MASTER PLAN: MASTER PLAN PROJECTIONS AND EXISTING SETTLEMENTS

23. Recent studies /9 indicate that the majority of urban households still rely on the informal housing market. In the example given above, it is likely that most of the new housing stock would be created by increasing densities and extending the areas of existing villages. Formal housing development, of the type financed by BTN, will occur in some of the areas zoned residential, and certainly outside them /10. The pattern of development in the year 2005 will be very different from the pattern shown on the master plan. The low and lower middle income population will be concentrated in villages densified at about 10 times the maximum density envisaged in the master plan. Formal housing will be scattered in areas around the existing road infrastructure network. The overall area occupied by housing will be much smaller -- because of the higher density -- than the area shown on the plan (see "affordable" estimate on Figure 2). The higher density of low income housing will most likely result in ground water pollution and unsanitary liquid waste disposal, because the sanitary network planned for much lower densities, will be unable to handle the increased stream of waste. However, if projection of densities had been based on current developments the primary infrastructure would have been different, much shorter (as less land needs to be developed for the population envisaged) but with higher standards to serve a population at higher desnsities.

24. In the above example, the master plan, or at least the part of the plan which would have been enforced through the granting of location permits, will have had a negative effect on the welfare of low income households. It will have increased the cost of developing land, and it will have failed to predict what type of infrastructure was needed and where it was needed. While master plans often have similar shortcomings in many other countries and have often shown to be biased against the poor, it does not need to be so. Master plans should be used as a forecasting tool rather than as a restraining straight jacket. Minimum land consumption per households should not be prescribed by master plans but should be established by market forces. Land prices could be reduced and made more affordable by increasing the supply of developable land. This could be done by reducing the regulatory constraints and through a better planning of infrastructure. Planners should aim at using master plans to guide the implementation of infrastructure and protect the environment at an affordable cost. Because of the way master plans are used in Indonesia, no legal change would be required to reorient them toward a more useful role. What is required is a change of approach and the development of a new physical planning methodology. This new methodology when developed would have to be disseminated through the Planning Department (Tata Kota) of the Ministry of Public Works, professional associations and teaching institutions.

/8 The other networks, water, sanitation, electricity and transport are not shown but follow the same pattern as the trunk roads shown on Figure 1-B.

/9 R.Struyk, "Summary Notes on Lower Income Housing Market in Urban Indonesia, October 1988.

/10 Developers start assembling land a long time in advance, often 3 to 5 years before developing it. Their priority in land selection is: (i) where there is demand; and (ii) close enough to an existing road (at a maximum distance of about 1.5 km). The zoning plan of the master plan is only an administrative hurdle and potentially an extra cost that the larger developers are used to handle.

II. PAST AND CURRENT WORLD BANK LENDING ACTIVITIES THAT ARE RELATED TO LAND REGULATORY ISSUES

25. In the long history of urban lending to Indonesia, the Bank has tried to address many of the regulatory land issues mentioned above. Project and sector lending and related technical assistance has been primarily focused on four types of interventions:

(a) Land information systems, mapping, studies of land regulations, housing, and land markets (Urban Land Information components of Urban Sector Loan and Urban III and IV, technical assistance of Housing Sector Loan);

(b) Reduction in the cost of minimum shelter (Technical assistance directed to Perumnas, Housing Sector Loan);

(c) Redistribution of infrastructure services directly to the informal sector in densely urbanized areas by obtaining a waiver from legal minimum standards (Kampung Improvement Program); and

(d) Improvement of the planning and design of metropolitan primary infrastructure, and thereby increase in the supply of urban land. (Urban Sector Loan).

A. "Relief Projects" Versus "Structural Change" Projects

26. In assessing the impact of Bank lending on the urban poor one has to differentiate between: (i) "structural change" projects aiming at a long range impact; and (ii) "relief" projects more narrowly focused on providing immediate benefits to selected target groups. A well-designed strategy should contain both types of intervention. The structural change projects are the ones which aim at pushing the informal/formal sector boundary down the income scale, or in other words, at increasing the proportion of households in the formal sector (see Figures 5-A and 5-B for a graphic representation of the two type of projects). The Land Information System components /11 of several urban projects and the Housing Sector Loan belong to this category. The relief projects are the ones that aim at benefiting the poor directly and immediately, without necessarily correcting the circumstances that created the inequity in the distribution of benefits. The Kampung Improvement Program (Figure 5-C) belongs to this category.

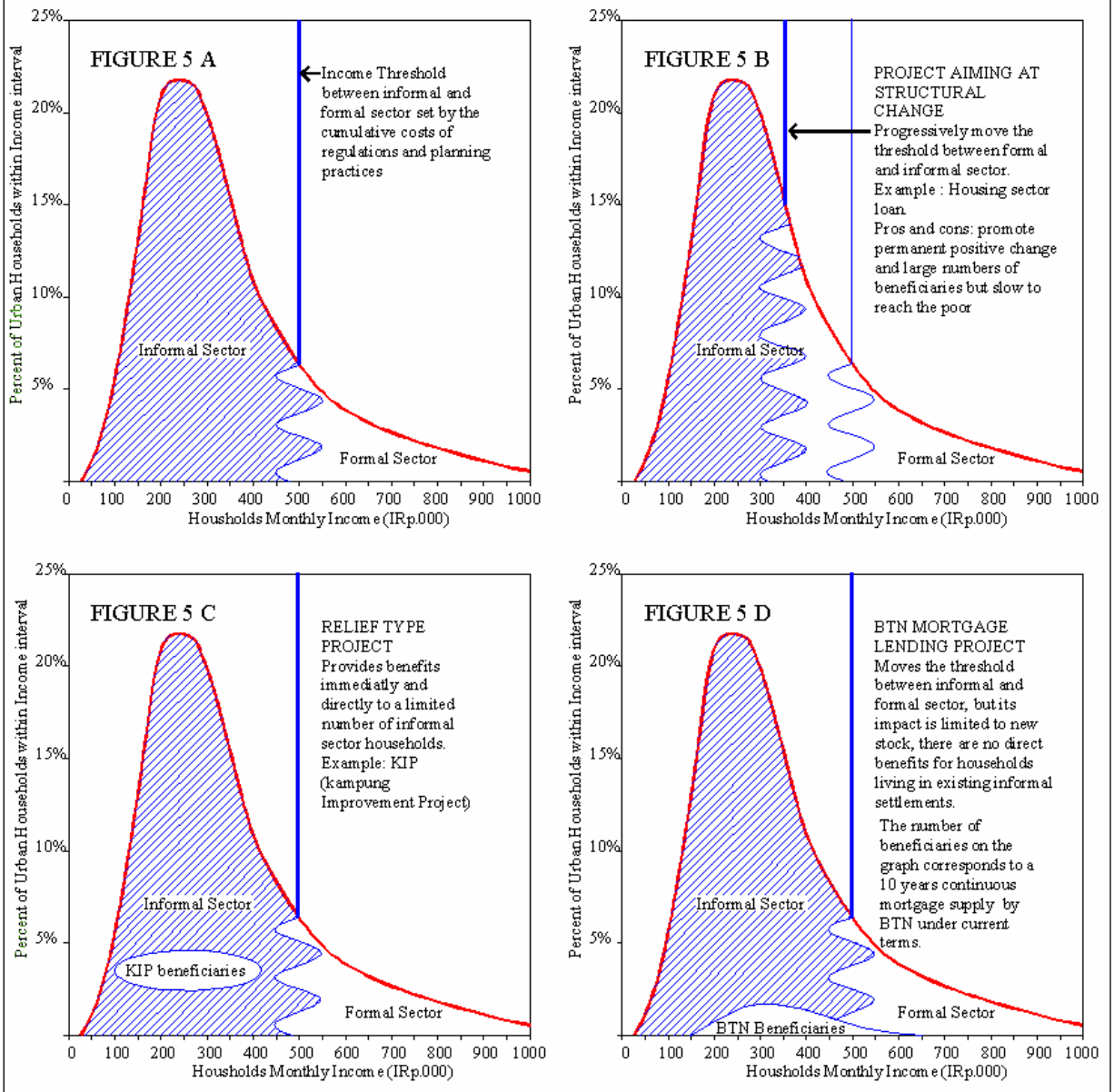
27. It is often tempting when trying to correct inequities through project or sector lending to consider that "relief" type projects are the only one which are genuinely focused on the poor. It is true that structural change projects are slow at reaching the poor, as they slowly nibble at the boundaries of the informal sector through adjustments in legislation, regulation, planning, and management practices. However, while the long-range projects are slow to reach the poor and have a tendency to reach the richest of the poor first, they bring along permanent changes that are correcting structural shortcomings in the functioning of institutions /12. Whereas short-range projects bring fast relief, but they are difficult to replicate, they often benefit a small number of households compared to the total number of households that would qualify as beneficiary, and they are vulnerable to budgetary reallocation.

/11 See B.Fisher, L. Holstein Memo- October 3, 1988 for a cross project assessment of LIAS activities in Bank project in Indonesia.

/12 "Structural changes" projects are not relying on a trickle down effect to reach the poor. They have to be aimed from the start at low income group, but they can reach the poor only at the pace allowed by institutional change.

FIGURE 5

IMPACT OF DIFFERENT TYPES OF URBAN PROJECTS ON THE INFORMAL SECTOR

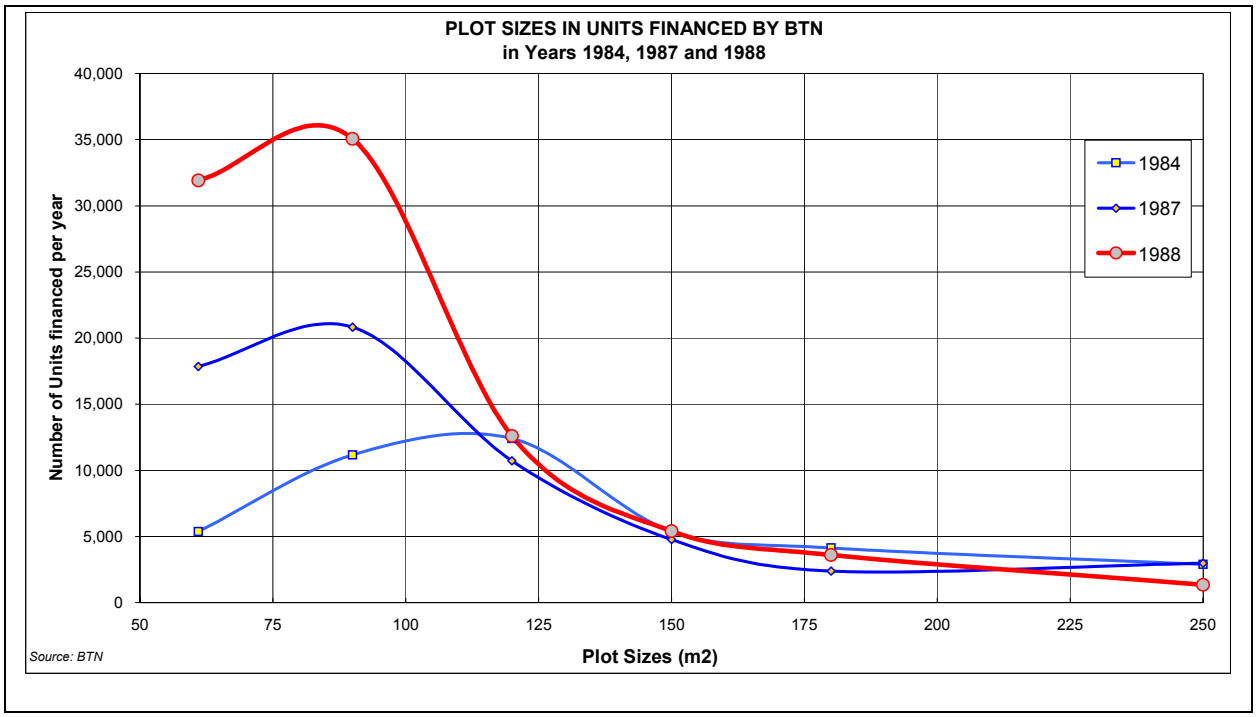


Sources: Income distribution curve (1988) derived from Urban Institute/Hasfarm "Choices & Opportunities: low income rental housing in Indonesia, Table 2.

28. The current debate about the income of households who benefit from BTN lending through the Housing Sector Loan is a good illustration of the dilemma between long range structural change and short range relief. There is no doubt that the Housing Sector Loan has succeeded in pushing back the limit between the formal and informal sectors by adjusting minimum shelter standards and getting the formal private sector to supply on a large scale housing units to households with no previous access to formal housing finance. Whether the households who benefit from BTN financing are at the 30th percentile or the 60th percentile of the income scale is irrelevant when assessing the long range impact of the project on the poor (see Figure 1). The important issue is whether the additional resources provided by the Bank loan had a permanent effect in giving access to housing finance to households that would not have qualified under the pre-project rules. The graph shown on Figure 6 illustrates a way of monitoring the real progress made by BTN in reaching lower income households. Plot sizes constitute a more accurate indicator than declared income to assess the real income of project beneficiaries. The number of loans provided to units on larger plots (above 100m2) has slightly decreased between 1984 and 1988 while the number of loans provided to units below 100 square meters has increased about three fold. Before the BTN projects there were no plots below 180 square meters supplied on the formal sector. Stimulated by BTN mortgage lending, developers have created new designs and addressed new markets that before project implementation were exclusively within the informal market system.

29. This type of structural adjustment projects are necessarily slow in reaching the poor because they aim at bringing permanent change. For instance, being able to respond to demand for formal housing finance from households between, the 25th to the 60th percentile would require an enormous increase in the volume of borrowing and lending capability of Indonesian banks (Figure 5-D and Figure 1). It is clear that this target could not be achieved before the present institutions improve their financial management practices and develop new and more effective borrowing instruments. For this reason, one has to acknowledge that amending legislation and minimum standards is not sufficient to reduce the number of households in the informal sector. Institutions, that in the past were providing benefits to a small clientele at the top of the income scale, would have to gradually adjust their operation to serve a much larger number of households. This applies to financial institutions such as BTN as well as to line agencies and institutions that are on the critical path for the delivery of subdivision permits.

FIGURE 6: DISTRIBUTION OF PLOT SIZES FINANCED BY BTN
BETWEEN 1984 AND 1988



30. Urban “relief” projects that benefit directly and immediately the poor are disadvantageously small in size and difficult to replicate due to the design and management skills required to keep them sharply focused on the original target group. In the history of Bank urban lending, the Kampung Improvement Programme had been a notable exception to this rule. KIP has managed to reach a significant number of poor and has passed the "pilot project" stage /13. However, KIP remains dependent on planned budget allocations for its sustenance. Fiscal year 1986 has showed a decline in real term in budgetary expenditure for poverty related programs such as KIP /14. While investment in KIP should be sustained, as it constitutes the most rapid way of redistributing services to the poor, other longer-range programs should be explored to stimulate the creation of infrastructure in new kampung areas under market conditions and independently from yearly budget allocations.

31. KIP has not addressed the problem of the planning and implementation of infrastructure for the poor in newly developed areas. The standards used for upgrading kampungs are not yet considered permissible in the suburban fringe. The present high densities in city core Kampung (up to 1200 people/ha) do not represent a case of "planning malpractice" nor do they show the result of "uncontrolled growth". Those high densities, corresponding to plots of about 30 square meters per family, are the direct consequence of land markets conditions with all the rigidities and distortions brought about by the combined effect of land legislation and infrastructure planning practice. The problem of high densities is compounded when urban planners deny the provision of infrastructure to newly formed Kampungs, because they do not conform to legal maximum densities based on ideals but unaffordable "needs", or they are located outside planned residential areas.

32. In addition, the benefits to the poor brought by projects aimed at improving the efficiency of primary urban infrastructure should not be underestimated. Those projects are not expressly aimed at the poor, but because they increase the supply of urban land, they benefit equally the informal and the formal sector. The provision of trunk infrastructure and in particular the improvement of the efficiency of the transport network is extremely important for the poor. By increasing the affordable radius of daily commuting for poor households, an improved transport network raise employment opportunities and improve shelter choices. Better urban transport is a more efficient way of keeping residential densities at reasonable comfort level than the current zoning laws on maximum density.

33. The opening of large area of undeveloped land for urbanization, which is the result of large scale infrastructure projects, should be followed with a reform of land use planning regulations and practices so that the problems which were corrected in the urban core through KIP do not appear again. Low-density kampung in suburban areas should be identified on master plans as potential low income residential zones.

B. Land Regulations and Planning Practices Issues to be Addressed in Future Urban Projects

34. A number of issues related to the land regulatory environment and the poor have not been addressed yet. Those issues are:

(a) How to make the present land subdivision legislation and practice less costly, more equitable, and less discriminatory against the poor;

(b) An overall assessment of the cost-benefits of urban planning legislation and practice, including an evaluation of the operating cost of legislation and its links with informal payment practices. This would be followed by a selective deregulation of urban land use and planning.

(c) The manner through which formal sector benefits, such as housing finance, could be passed to the informal

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/13 At the end of Pelita IV, around 540,000 households have received benefits from the KIP programme out of about 10.4 million households in urban areas. (LAPTRI: "Final Report on Urban Housing Improvement Loans") Cipta Karya, 1987.

/14 "Indonesia- Urban Poverty Alleviation Strategy Options", Paul R. Stott memorandum June 9, 1988.

sector through the development of new savings and lending instruments;

(d)The development of an urban planning methodology which would take the poor into account when projecting infra-structure and social services in fringe urban areas; and

(e)The development of short range infrastructure projects specifically aimed at the informal shelter market in urban fringe areas.

III. PROPOSED AGENDA FOR MODIFICATION OF SOME ASPECTS OF LAND LEGISLATION AND PLANNING PRACTICES THAT HAVE AN IMPACT ON THE POOR

35. In devising an agenda for improving the land regulatory framework, it is important to differentiate and keep a balance between relief/immediate impact type of projects and long range/-structural change projects.

A. Land Titling, Mapping and Land Information Systems

36. In the long range, present Bank effort in mapping titling and building land information system should be continued but those measure will take a long time to have an impact on the poor. As an intermediate range solution: explore ways of extending formal sector benefits to informal land titles (housing and business finance)

37. Relief/immediate impact. Research should explore how to quickly provide some of the benefits of the formal titling systems to informal types of tenure. Many informal types of land titles are providing an adequate security of tenure but they do not allow the use of land as collateral for a business loan or a mortgage. The acceptability of a semi-formal type of tenure that gives access to the formal financial system needs exploring. However, one should recognize that the effect on the poor of this type of measure would be severely limited by the managerial capacity of financial institutions to extend its borrowing capacity and to lend to a new type of customer.

38. Long range/structural change. Formal cadastre: The present stream of studies and project components aiming at developing a modern land titling system are the necessary counterparts of relief measures suggested above. Because those projects require a gradual building-up of institutional capability, they would take time to give results and have an impact on the poor. Mapping and land information systems. The mapping and land information systems exercises carried out under the Urban Sector Loan and Urban IV are important inputs in cadastre projects, and for the reform in planning methodology proposed below. The photomaps produced under Urban IV are ideal documents to reorient planners toward the realities of urban development and away from the abstractions of zoning and regulated densities. The continuation of this program needs more support and an emphasis is needed to widely distribute the maps produced.

B. Affordability of Minimum Standards

39. The following steps could be followed to improve the affordability of minimum standards:

(a)Keep pressing to review the minimum standards used by the formal housing finance system (BTN). Expand the capacity and efficiency of the formal housing finance system;

(b)Reduce the cost of land development for private sector by:

(i) simplify legislation and building permit process; review operation cost of new system;

(ii) opening up more land through strategic primary and secondary infrastructure investment;

(c)Recognize the limited role of the public sector in the supply of new shelter affordable to low income group;

(d)Acknowledge that the private sector is presently producing affordable units in suburban villages, extend the

benefits of the formal sector to those villages to accelerate densification.

(e)Deregulate on plot development; and

(f)Encourage densification of Kampung through proper access infrastructure.

40. Informal Sector Land Use and Plot Development Standards. Recent studies /15 have shown that there is a vigorous informal housing market in newly developing urban areas. This market includes a great variety of tenure arrangements and also includes cheap rental housing. The housing units produced by the informal supply system show a vast array of standards which are by definition affordable to every category of poor households. Those standards are the product of market conditions under the constraints imposed on the informal sector. The most important constraints are: (i) the lack of access to the formal saving/borrowing financial system; and (ii) the lack of infrastructure linking informal settlements with the formal primary network.

C. Distortion of Land Markets

41. The following steps could be taken to reduce the distortions of land markets:

(a)Review land use category, objectives, costs and benefits of land use permit as practices by Central Government Agencies, local authority and Tata Kota;

(b)Improve land use mapping and land use information system;

(c)Put more emphasis on monitoring of land market than on land use control measures;

(d)Eliminate density regulations, concentrate on affordable and manageable environment protection regulations;

(e)Revise zoning laws, concentrate on environment issues, do not attempt to control densities. Densities should be carefully monitored but they should not be regulated (with the exception of the FAR in CBD areas); and

(f)Use infrastructure investments to open a maximum of land for development at the lowest cost.

42. A complete evaluation of zoning and densities legislation, regulation and practice should be conducted. Any regulation whose objective and benefits are unclear should be discarded. The new legislation should concentrate its control effort on few environmental issues that are important. The operating cost of any legal control on development should be correctly assessed.

D. Distortion in the Distribution of Urban Services

43. The following steps should be taken to improve efficiency and equity in the distribution of urban services:

(a)Review methods to develop infrastructure investment program in metropolitan areas;

(b)Target part of new infrastructure in suburban areas to existing villages;

(c)Disseminate projected land use map with projected densities (based on densities of current settlements) and income groups to all line agencies;

(d)Revise master plan preparation techniques, in particular:

/15 "Summary Note on Lower Income Housing markets in Urban Indonesia", R. Struyk, October 1988.

(i) project densities based on affordability rather than on density control; and

(ii) disseminate existing and projected land use plans to line agencies to allow them to plan infrastructure taking into account existing network of kampungs;