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HONDURAS

ADOPTION OF MOBILE TECHNOLOGY TO BOOST THE HONDURAN ECONOMY

(HO-T1263)

DONORS MEMORANDUM

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CONTENTS

PROJECT SUMMARY EXECUTIVE SUMMARY

I.	PROBLEM TO BE ADDRESSED	1
II.	THE SOLUTION	2
III.	ALIGNMENT WITH THE IDB GROUP, SCALABILITY, AND PROJECT RISKS	5
IV.	COST AND FINANCING	5
V.	PROJECT EXECUTING AGENCY AND IMPLEMENTATION STRUCTURE.....	6
VI.	FULFILLMENT OF MILESTONES AND SPECIAL FIDUCIARY ARRANGEMENTS	8
VII.	ACCESS TO INFORMATION AND INTELLECTUAL PROPERTY	8

PROJECT SUMMARY

ADOPTION OF MOBILE TECHNOLOGY TO BOOST THE HONDURAN ECONOMY (HO-T1263)

Honduras, like many of the region's countries, still faces challenges in terms of access to products and financial services, especially low-income populations and those in rural areas. Even though mobile technology has been adopted and scaled up in other countries as a means of facilitating transaction banking in economies, the use of cash still prevails in Honduras, which generates high costs for suppliers and users of those products and services.

The objective of this project is to facilitate access to financial services primarily for middle- and low-income Hondurans through the development of an innovative model based on a mobile technology platform that will enable financial institutions to conveniently, efficiently, and securely provide their service offering to populations in both urban and remote, rural areas of Honduras. This platform will also promote innovation, entrepreneurship, and economic growth by offering public and private institutions from various sectors (health, basic services, agriculture, trade, agroindustry, etc.) the opportunity to enhance their business processes related to bank transactions, cutting the risks associated with handling cash.

The company Telefónica Celular S.A. de C.V. (hereinafter "CELTEL," "Tigo," or "Tigo Honduras") is the leading provider of cellular telephony services in the country with a market share of 67%. Tigo Honduras will develop the proposed platform by using its current technology infrastructure as a starting point. As part of this project, financial education campaigns will also be undertaken both for Tigo staff and the general public, and the development of a favorable regulatory environment will be promoted for business models that favor financial inclusion based on the use of mobile technology.

As a result of the project, at least seven financial institutions will be able to adopt mobile technology to expand their services, especially in areas that lack access to financial services, thus enabling more than 98,000 medium- and low-income people throughout Honduras, including people in the informal sector or self-employed workers, to have access to formal banking services and financial services through the use of mobile technology.

This would be the first initiative in the Honduran economy in which financial institutions form partnerships with telecommunications service providers to adopt mobile technology as a means of reaching their customers, thus increasing their efficiency, scope, and profitability, while allowing end customers to conveniently perform banking transactions and enjoy greater security by reducing the use of cash.

This project is aligned with the IDB Country Strategy with Honduras as it promotes the development of productive sectors through the private sector and facilitates access to financial services. It is also aligned with the work undertaken by the Capital Markets and Financial Institutions Division (CMF), aimed at supporting efforts to digitize the economies of the region and to promote the adoption of financial inclusion strategies.

ANNEXES

Annex I	Results Matrix
Annex II	Summary Budget

APPENDICES

Proposed resolution

INFORMATION AVAILABLE IN THE TECHNICAL DOCUMENTS SECTION OF THE MIF PROJECT INFORMATION SYSTEM

Annex III	Itemized budget
Annex IV	Diagnostic needs assessment of the executing agency (DNA)
Annex V	Project status reports (PSRs), fulfillment of milestones, fiduciary agreements, and institutional integrity
Annex VII	Contingent-recovery technical cooperation term sheet

ABBREVIATIONS

BCH	Central Bank of Honduras
CACIL	Cooperativa de Ahorro y Crédito Intibucana Limitada
CMF	Capital Markets and Financial Institutions Division
CNBS	National Banking and Insurance Commission
DNA	Diagnostic needs assessment
ELGA	Cooperativa de Ahorro y Crédito de los Empleados Locales del Gobierno Americano [U.S. government employee credit union]
FAMA	Financiera FAMA
IDH	IDH Microfinanciera
IHNDEI	Instituto Hondureño de Estudio y Desarrollo Integral de la Comunidad [Honduran Institute for the Study and Comprehensive Development of the Community]
MIF	Multilateral Investment Fund
Tigo or	
Tigo Honduras	Telefónica Celular S.A. de C.V.
Tigo Money	Business model of the company Servicios, Productos y Negocios S.A. de C.V. – SERPRONSA – part of the Tigo Honduras Group

EXECUTIVE SUMMARY

ADOPTION OF MOBILE TECHNOLOGY TO BOOST THE HONDURAN ECONOMY (HO-T1263)

Country and geographic location:	This project will have national coverage.		
Executing agency:	Telefónica Celular S.A. de C.V.		
Focus area:	Knowledge economy		
Coordination with other donors/Bank operations:	Inter-American Investment Corporation (IIC).		
Project clients:	This project will benefit 98,000 people and 7 financial institutions in Honduras.		
Financing:	Contingent-recovery technical cooperation funding:	US\$310,000	
	Nonreimbursable technical cooperation funding:	US\$165,000	
	Investment:		
	Loan:		
	Other (explain):		
	Total MIF contribution:	US\$475,000	33%
	Counterpart:	962,996	67%
	Cofinancing (if applicable, include a separate line for IDB cofinancing):		
	Total project budget:	US\$1,437,996	100%
Execution and disbursement period:	36 months for execution and 42 months for disbursements.		
Special contractual conditions:	The following will be conditions precedent to the first disbursement: (i) appointing a project coordinator; and (ii) submission to the Bank of the memorandum of understanding signed between Tigo Honduras and at least three of the seven participating financial institutions.		

**Environmental
and social
impact review:**

This operation has been pre-evaluated and classified on 3 October 2016 in accordance with the requirements of the IDB's Environment and Safeguards Compliance Policy (Operational Policy OP-703). Since the impacts and risks are limited, the project is proposed for classification as a category "C" operation.

I. PROBLEM TO BE ADDRESSED

Problem description

- 1.1 Honduras, like many of the region's countries, still faces challenges in terms of access to products and financial services, especially low-income populations and those in rural areas. According to the Global Findex Database,¹ 30% of the Honduran population claims to have a bank account, whereas the Latin American average is 51%. In rural areas, the difference is even greater: 2.6 people out of 10 in Honduras have a bank account, while in Central America, the rate is 4.6. As for savings accounts and credit at a formal financial institution, the percentages recorded in Honduras are 14% and 10%, respectively, which are considered low compared to the Latin American average, but are similar to levels seen in Central America (13% and 11%).
- 1.2 The Honduran financial system is characterized by being concentrated in four institutions that account for almost 60% of the system's assets and by having limited service coverage. In 2014, there were 3,137 points of service at supervised financial institutions;² most of them (54%) are concentrated in the departments of Francisco Morazán and Cortés.³ The number of points of service per 10,000 adults is very low (6.8) and shows little growth over the past five years (5.7 in 2010). The strategies for expanding financial services coverage have traditionally been based on establishing branches. However, these strategies have high investment and maintenance costs for financial institutions, rendering them commercially unviable. As a result, other distribution channels are now being explored, such as mobile banking and electronic money. A study by the National Telecommunications Commission (CONATEL) showed that the penetration of mobile telephony in Honduras is currently 87.57%, which creates great potential for use as a financial inclusion instrument in the country.
- 1.3 Even though mobile technology has been adopted and scaled up in other countries as a means of facilitating transaction banking in economies, the use of cash still prevails in Honduras, which generates high costs for suppliers and users of products and services, as well as creating risks due to the citizen insecurity in the country.
- 1.4 As a result of the project, financial institutions will be able to expand their services throughout the country, delivering their offering to areas currently lacking access to financial services. As a result, more than 98,000 middle- and low-income people, including people in the informal or self-employed sectors, will have the opportunity to access financial services.

¹ Demircug-Kunt, A. and L. Klapper, "Measuring Financial Inclusion: The Global Findex Database" World Bank Policy Research Working Paper 6025, World Bank, Washington, D.C, 2012.

² Of these points of service, 90% are commercial banks, 3% are financial corporations, and 2% are development finance organizations.

³ Financial inclusion bulletin: Honduran financial system, National Banking and Insurance Commission (CNBS), 2013.

II. THE SOLUTION

A. Project description

- 2.1 This project aims to provide the Honduran population access to financial services. To do so, a mobile technology services platform-based model already developed by Tigo Money,⁴ a business unit of Tigo Honduras, will be implemented. Through this platform, financial institutions will be able to conveniently, efficiently, and securely deliver their services using mobile technology to both urban and rural/remote populations in Honduras.⁵ Thus, the project will contribute to promoting financial inclusion in the region by providing end customers access to financial services offered by recognized financial institutions.
- 2.2 The platform considers the development of a portfolio of services aimed at 5 banks and microfinance institutions to undertake transactions that involve the transfer of funds between their customers' electronic wallets and accounts (savings, payments, deposits, loan repayments and disbursements, etc.). It also includes a financial services offering aimed at public and private institutions in a number of sectors (health, basic services, agriculture, trade, agroindustry, etc.), which will enable them to innovate and enhance their business processes related to bank transactions, while reducing the risks associated with handling cash. These services include: (i) *mass disbursements*, a product that enables institutions to make partial/full payments of salaries, travel allowances, bonuses, commissions, awards, or loan disbursements through deposits made into employees' electronic wallets; (ii) *payments to businesses*, through which partner businesses accept payments from their customers by means of electronic funds transfers; and (iii) *collection offices*, consisting of the collection of money for companies that focus on the mass sale of products and/or that involve a payment.
- 2.3 A key component in the Tigo Money model is Banco Atlántida, a strategic partner which, through a trust fund, backs 100% of the electronic money in circulation. Banco Atlántida performs a process converting the equivalent in national currency into electronic money and vice versa. The conversion takes place using security mechanisms between the Banco Atlántida and Tigo Money platforms, with each electronic money unit equivalent to one Honduran lempira.
- 2.4 **Proposed model/solution.** The platform to be implemented under the project is based on the technology infrastructure currently available on Tigo Money for providing financial services. It will consider the flexibility needed to adapt to the requirements of each financial institution and will also have functions to ensure easy integration and interoperability with the support systems for the financial services to

⁴ Tigo Money is a business model of the company Servicios, Productos y Negocios S.A. de C.V. – SERPRONSA, part of the Tigo Honduras group, which functions as the business unit through which Tigo Honduras currently offers services enabling people who have no nearby bank branch to undertake financial transactions rapidly and securely using their cellular phone. Through its distribution network, it is possible to exchange cash for electronic money that can then circulate through customers' electronic wallets and eventually leave the system in an exchange of electronic money for cash. Tigo Money currently has more than one million customers nationwide who can make payments and transactions through their electronic wallets on a recurring basis.

⁵ According to the 2016 Permanent Multipurpose Household Survey by the Honduran National Statistics Institute, 85.3% of rural households have a cellular telephone versus 95% of urban households.

be offered by each financial institution. The services to be offered will be accessible from mobile phones via text messaging (SMS) services or over the Internet (smartphones). In addition to technology development, alternative business models will be analyzed for managing and operating the platform that ensure a win-win scenario for all actors (Tigo, financial institutions, customers).

- 2.5 The project also includes capacity-building among Tigo staff and campaigns targeting the general public to promote the adoption of the developed services, and actions to promote the generation of a favorable regulatory environment for developing similar models where financial institutions and technology companies come together to contribute to the promotion of financial inclusion.
- 2.6 The project starts with a pilot phase, the results of which will make it possible to make the adjustments needed to expand it to other financial institutions. Tigo has already begun negotiations with Honduran financial institutions interested in using mobile telephony as a means of expanding their offer and improving their services. These institutions include Banco Popular, Credisol, IDH Microfinanciera (IDH), Instituto Hondureño de Estudio y Desarrollo Integral de la Comunidad [Honduran Institute for the Study and Comprehensive Development of the Community] (IHNDEI), Financiera FAMA (FAMA), Cooperativa de Ahorro y Crédito de los Empleados Locales del Gobierno Americano [U.S. government employee credit union] (ELGA), and Cooperativa de Ahorro y Crédito Intibucana Limitada (CACIL). Tigo also provides the possibility for the project to replicate this telecommunications-financial institutions model through its network presence in other countries of the region, including other Central American countries.
- 2.7 The project is in compliance with the Honduran regulatory framework for authorization and operation of nonbanking institutions that provide payment services using electronic money (INDELE), issued by the Central Bank of Honduras (BCH) on 24 February 2016.⁶ These regulations allow transactions to be performed using electronic money through mobile devices as a means of promoting financial inclusion. Authorized services include the activation of the electronic wallet, sending and receiving electronic money, transfers between users, purchases of goods and services (known as merchant payments), collection management services, payments to suppliers, and payment of salaries and wages (known as mass payments). On 8 July 2016, the National Banking and Insurance Commission (CNBS) also issued the rules for the supervision of nonbanking institutions that provide payment services using electronic money (INDEL) in Circular 024/2016.
- 2.8 **Innovation.** The innovation of the proposed model is based on the connection of the current Tigo Money service platform to the network of financial institutions, which will have a multiplier effect on financial inclusion and the benefits thereof for low-income rural and urban populations. The incorporation of the financial institutions into the model also requires their participation in determining the more appropriate mechanisms for handling the conversion of electronic money and cash and to back, safeguard, and administer the funds that will circulate through the ecosystem created by the project.

⁶ Tigo Honduras is in the process of adapting to the regulations and amendments issued by the BCH and the CNBS, for which 30 November 2016 has been set as the date for completing this process.

- 2.9 This would be the first initiative in the Honduran economy in which financial intermediaries form partnerships with telecommunications service providers to adopt mobile technology as a means of reaching their customers, thus increasing their efficiency, scope, and profitability, while also allowing greater economic spillover to the 3,800 SMEs that make up the Tigo Money agents network.

B. Project components

- 2.10 Component I: Development, pilot project, and expansion of mobile technology to provide financial services. This component includes the performance and pilot testing of adaptations to the Tigo Money technology platform that will make it interoperable with the platforms of the three participating financial institutions. This component also includes actions to adjust the platform based on the results of the pilot and its subsequent expansion to other financial institutions.
- 2.11 Component II: Promotion of the adoption of financial services offered via mobile technology. This component will build capacities among Tigo Money agents to promote the developed services. To do so, a training program will be developed aimed at generating standard, clear, concise messages to facilitate communication of the services' characteristics, usefulness, and advantages to end customers. Communication campaigns will also be undertaken targeting end customers.
- 2.12 Component III: Development of the ecosystem. This component will involve work with government authorities to develop a regulatory environment conducive to the use of mobile technology by financial institutions and their customers. It also considers the strengthening of protection mechanisms for consumers who access financial services through mobile technology.
- 2.13 Component IV: Knowledge and dissemination. This component will finance a case study on the use of mobile financial services in Honduras, including the lessons learned that are useful for developing similar models in Latin America and the Caribbean. The development of an international information exchange event will be financed on the provision of mobile financial services.

C. Project outcomes, impact, monitoring, and evaluation

- 2.14 The project will create an interconnected economy that facilitates transaction banking, cutting costs for suppliers and users of products and services. This project will also enable different sectors, such as health, basic services, agriculture, trade, and agribusiness, to facilitate the payment of items including salaries, loan repayments, public utilities, and taxes.
- 2.15 The expected outcomes of project implementation are: (i) 98,000 subscribers accessing financial services through mobile technology (210400); (ii) 1,500,000 transactions performed using mobile technology; and (iii) seven financial institutions adopt mobile technology to provide services (230100).
- 2.16 Tigo Honduras will use robust information systems to evaluate project progress and to take necessary corrective measures during project implementation. In addition, it will periodically report project progress through the Project Status Report system and on the final project outcomes through the Project Completion Report. This project will include a midterm and final evaluation.

III. ALIGNMENT WITH THE IDB GROUP, SCALABILITY, AND PROJECT RISKS

A. Alignment with the IDB Group

- 3.1 This project is aligned with the work of CMF, specifically its efforts to digitize the economies of the region and to promote the adoption of financial inclusion strategies. CMF also advises IDB member countries on the formulation and implementation of comprehensive strategies to digitize and adopt new technologies, infrastructures, business models, and institutional frameworks for productive development in the region. This project could provide feedback on the process of developing regulatory frameworks and benefiting from them after their implementation.
- 3.2 This project is also framed within the IDB Country Strategy with Honduras to promote the development of productive sectors through the private sector and to facilitate access to financial services in the country.

B. Scalability

- 3.3 Given the national presence of Tigo Honduras through its network of agents and the partnerships expected with financial institutions, including commercial banks and microfinance institutions, this project has high potential to be scaled up nationally. The model to be developed under this project could be considered by the Bank and the Government of Honduras for the payment of conditional cash transfers, as it makes the transaction secure. The lessons learned from this intervention could be transferred to other countries in the region where Tigo also has a presence.
- 3.4 The activities to scale up the project are incorporated under Component I and will be implemented upon completion of the pilot phase. These expansion activities, which include training Tigo staff and implementation of a communications campaign, will be financed in full by Tigo Honduras.

C. Project risks

- 3.5 The following factors could have a negative impact on the implementation of project activities: (i) Honduras lacks regulations making it possible to open bank accounts using a cellphone, which could limit the development of the electronic wallet product. Mitigation measures: a project component promoting the development of a regulatory environment conducive to the use of mobile technology by financial institutions; (ii) low uptake of the developed services. Mitigating measures: a project component encouraging customers to discover and familiarize themselves with the financial services offered through the platform; (iii) lack of availability and interest from points of sale to provide information on options and use of financial services. Mitigation measures: during design of the training program, actions on the importance of the agents' role in expanding the services will be considered.

IV. COST AND FINANCING

- 4.1 The project has a total cost of US\$1,437,996. The MIF will contribute US\$475,000 (32%) of that amount, and the counterpart will contribute US\$962,996 (68%). The MIF financing will include: (i) contingent-recovery technical-cooperation funding totaling US\$310,000, in accordance with the terms included in Annex VII; and (ii) US\$165,000 in nonreimbursable technical-cooperation funding to cover the costs

of Components III and IV and activities related to evaluations, legal fees, and ex post reviews.

- 4.2 The contingent-recovery technical-cooperation funding (US\$310,000) will be used as a financing mechanism for this project, aimed at testing the viability of mobile telephony as a means of facilitating sustainable access to financial services across Honduras. This financing is interest free and repayment is contingent upon the successful implementation of the project (see Annex VII).

	MIF	Counterpart	Cofinancing	Total
Project components				
Component 1: Development, pilot project, and expansion of mobile technology to provide financial services	126,632	711,444		838,076
Component 2: Promotion of the adoption of financial services offered via mobile technology	133,868	133,667		267,535
Component 3: Development of the ecosystem	60,000			60,000
Component 4: Knowledge and dissemination	30,000			30,000
Project management (costs of the execution unit)	49,500	97,500		147,000
Midterm and final evaluations (*)	40,000			40,000
Ex post reviews (*)	5,000			5,000
Audited expense statements	10,000			10,000
Legal fees (*)	20,000			20,000
Contingencies		20,385		20,385
Grand total	475,000	962,996		1,437,996
% of financing	33%	67%		100%

(*) Resources administered by the MIF.

V. PROJECT EXECUTING AGENCY AND IMPLEMENTATION STRUCTURE

A. Description of project partner

- 5.1 Tigo Honduras will be this project's executing agency and will sign the agreement with the Bank. Tigo Honduras is the main provider of cellular telephony services in the country, with a 67% market share (4.5 million users nationwide). Tigo Honduras is part of Millicom,⁷ a global telecommunications group headquartered in Luxembourg, currently offering mobile telephony services to 270 million people in 13 countries in Latin America and Africa and that has grown based on entrepreneurship and innovation. The institutional mission of Millicom is the digital transformation of Honduras, through its innovative products and services offering.⁸
- 5.2 The project will be implemented by Tigo Money, a business unit of Tigo Honduras⁹ that currently offers cellular phone-based transaction services. Tigo Money's cellular service covers 92% of Honduras, through 2,900 points of sale across the country's

⁷ Millicom is part of Investment AB Kinnevik ("Kinnevik"), a lead investment group in Sweden that invests in the mobile telecommunications sector, e-commerce, entertainment, and financial services. Source: <http://www.millicom.com/who-we-are/our-growth-story/>.

⁸ <http://www.millicom.com/where-we-operate/#honduras>.

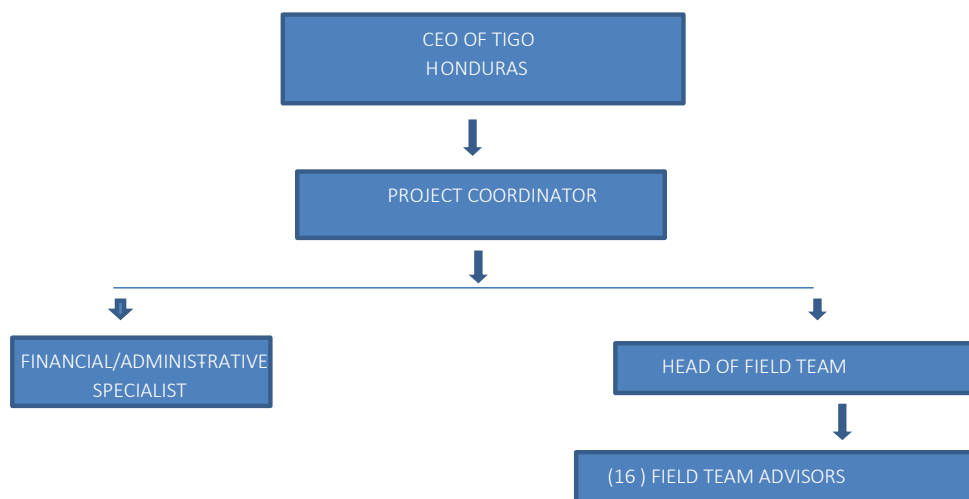
⁹ Tigo Honduras has four business units: Tigo Start, Tigo Business, Tigo Móvil, and Tigo Money.

18 departments and more than 275 municipios, and it is the sole operator that offers electronic money services. In December 2015, Tigo Money had 1 million users, accounting for 22% of Tigo Honduras users.

- 5.3 The IDB/MIF has experience working with other Millicom group companies. With Tigo Paraguay, it carried out a technical cooperation project “Provision of mobile financial services under the ‘Last Mile’ business model” under the regional “Technology for Increased Access to Finance” program TEC-IN (RG-M1155). The objective of this operation was to develop and promote the use of the mobile wallet product as a channel for financial inclusion. In March 2015, this project had 1.25 million active users, 27% of Paraguay’s adult population, a level of penetration similar to that of the formal financial system in Paraguay.
- 5.4 Other partners involved in the implementation of this project are financial institutions (commercial banks, cooperatives, and microfinance institutions), which will adopt mobile technology to expand the coverage of their financial services. These potential partners include Banco Popular, Credisol, IDH, IHNDEI, FAMA, ELGA, and CACIL.

B. Structure and Implementation Mechanism

- 5.5 Tigo Honduras will delegate responsibility for the technical, operational, and administrative execution of the project to Tigo Money, which will establish an execution unit with the structure needed to execute the project activities and to effectively and efficiently manage resources. The execution unit will be made up of a project coordinator, a financial/administrative specialist, a head of field efforts, as well as technical staff specialized in providing advisory support in the field, as indicated in the following organizational chart:



- 5.6 The execution unit will be responsible for: (i) the comprehensive management of the project’s financial, administrative, and technical matters; (ii) the operational monitoring of project activities; (iii) the design, implementation, and execution of the annual work plan; (iv) the organization and maintenance of the program’s administrative files; (v) the project procurement and contracting, including preparation of terms of reference and the supervision and coordination of contracted

consultants; (vi) the control of budget management; (vii) the processing of requests to disburse the Bank's contribution; (viii) the preparation of the financial statements for the resources used; (ix) the presentation of administrative and technical reports to the MIF; (x) the coordination of the necessary actions with the different project actors; (xi) the revision and proposal of changes to the operating regulations; and (xii) raising awareness of actors and the dissemination of results.

VI. FULFILLMENT OF MILESTONES AND SPECIAL FIDUCIARY ARRANGEMENTS

- 6.1 **Results-based disbursements and fiduciary arrangements.** The executing agency agrees to the management, technical, and operational agreements entered into between the parties (executing agency and the IDB/MIF) concerning results-based disbursements, procurement, and financial management, as indicated in Annex V. Disbursements under the project will be contingent upon verification of the fulfillment of certain milestones, based on the means of verification agreed upon by the execution unit and the MIF. Fulfillment of milestones does not exempt the execution unit from the commitment of fulfilling the project's logical framework indicators and objectives.
- 6.2 Under the risk and performance-based project management modality, the amounts of the project disbursements will be established in accordance with the project's liquidity needs estimated for a maximum of six months. These needs will be agreed upon between the MIF and the executing agency and will reflect the activities and costs programmed in the annual planning exercise. The first disbursement will be contingent upon fulfillment of certain conditions precedent, and successive disbursements will be made provided the following two conditions have been met: (i) verification by the MIF that the milestones have been reached, as agreed in the annual planning document; and (ii) the execution unit has justified at least 80% of the cumulative advances of funds.
- 6.3 **Procurement and contracting.** For the procurement of goods and consulting services, the execution unit will be governed by the IDB's procurement policies (documents GN-2349-9 and GN-2350-9), in accordance with the market practices for the private and business sectors that are acceptable to the Bank.

VII. ACCESS TO INFORMATION AND INTELLECTUAL PROPERTY

- 7.1 **Intellectual property.** The IDB will hold the intellectual property to all works produced and/or results obtained under this project's nonreimbursable technical cooperation component. The Bank may, at its discretion, award a free, nonexclusive, noncommercial license for the dissemination, reproduction, and publication in any medium of any of these works that are exclusive property of the Bank. The executing agency will ensure that all the contracts entered into with consultants under this operation include the express assignment to the Bank of all copyrights, patents, and any other intellectual property right.