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BRAZIL

**PROCIDADES-RECIFE
DOWNTOWN RECIFE URBAN RENEWAL PROGRAM
(BR-L1190)**

LOAN PROPOSAL LOAN PROPOSAL

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ELECTRONIC LINKS	
REQUIRED	
1.	Annual work plan (AWP) http://idbdocs.iadb.org/wsdocs/getDocument.aspx?DOCNUM=2214331
2.	Monitoring and evaluation plan http://idbdocs.iadb.org/wsdocs/getDocument.aspx?DOCNUM=36358634
3.	Environmental and social management report (ESMR) http://idbdocs.iadb.org/wsdocs/getDocument.aspx?DOCNUM=2194331
4.	Procurement plan http://idbdocs.iadb.org/wsdocs/getDocument.aspx?DOCNUM=2214091
OPTIONAL	
1.	Economic viability study http://idbdocs.iadb.org/wsdocs/getDocument.aspx?DOCNUM=2199333
2.	Financial analysis http://idbdocs.iadb.org/wsdocs/getDocument.aspx?DOCNUM=2213873
3.	Institutional analysis http://idbdocs.iadb.org/wsdocs/getDocument.aspx?DOCNUM=2194344
4.	Relatório de avaliação ambiental [environmental assessment report] (RAA) http://idbdocs.iadb.org/wsdocs/getDocument.aspx?DOCNUM=2199323
5.	Resettlement plan http://idbdocs.iadb.org/wsdocs/getDocument.aspx?DOCNUM=2199519

ABBREVIATIONS

AWP	Annual work plan
CEMEI	Centro municipal de educação infantil [municipal early childhood learning center]
CSURB	Companhia de Serviços Urbanos do Recife [Recife Urban Services Company]
EIRR	Economic internal rate of return
EMLURB	Empresa de Limpeza e Manutenção Urbana [Urban Sanitation and Maintenance Company]
ESR	Environmental and Social Impact Review Secretariat
GCI-9	Ninth General Capital Increase, or Ninth General Increase in the Resources of the Inter-American Development Bank
HDI-M	Municipal Human Development Index
IBGE	Instituto Brasileiro de Geografia e Estatísticas [Brazilian Institute of Geography and Statistics]
LCF	Local Currency Facility
NCI	Net current income
OC	Ordinary Capital
PCR	Project completion report
PCU	Program Coordination Unit
PMR	Prefeitura Municipal de Recife [Municipal Government of Recife]
PRI	Perímetro de reabilitação integrada [integrated rehabilitation perimeter]
PSF	Posto de saúde da família [family health center]
SAS	Secretaria de Assistência Social [Social Assistance Department]
SCTDE	Secretaria de Ciência, Tecnologia e Desenvolvimento Econômico [Science, Technology, and Economic Development Department]
SDHSC	Secretaria de Direitos Humanos e Segurança Cidadã [Human Rights and Citizen Security Department]
SEBRAE	Serviço Brasileiro de Apoio às Micro e Pequenas Empresas [Brazilian Microenterprise and Small Business Support Service]
SEEL	Secretaria de Educação, Esporte e Lazer [Education, Sports, and Recreation Department]
SEFIN	Secretaria de Finanças [Finance Department]
SEHAB	Secretaria de Habitação [Housing Department]
SENAI	Serviço Nacional de Aprendizagem Industrial [National Industrial Training Service]
SCDUO	Secretaria de Controle e Desenvolvimento Urbano e Obras [Department of Oversight, Urban Development, and Works]
SS	Ministry of Health
UNDP	United Nations Development Programme
URB RECIFE	Empresa de Urbanização do Recife [Recife Urban Development Corporation]

PROJECT SUMMARY

BRAZIL PROCIDADES-RECIFE DOWNTOWN RECIFE URBAN RENEWAL PROGRAM (BR-L1190)

Financial Terms and Conditions					
Borrower: Município of Recife Guarantor: Federative Republic of Brazil Executing agency: Empresa de Urbanização do Recife [Recife Urban Development Corporation] (URB RECIFE)		Amortization period:		25 years	
		Grace period:		5 years	
		Inspection and supervision fee:		*	
		Interest rate:		Libor	
Source	Amount (US\$)	Disbursement period:		4 years	
IDB (Ordinary Capital)	20,015,000	Credit fee:		*	
Local	20,015,000	Currency of approval:		U.S. dollars from the OC**	
Total	40,030,000	Conversion into Brazilian reais:		Local Currency Facility (LCF)	
Project at a Glance					
Objective: To promote urban renewal in downtown Recife, with a view to enhancing the city’s economic and territorial dynamic through urban improvements and economic and social development actions, thus improving the quality of life for the city’s inhabitants.					
Special contractual execution conditions precedent to the first disbursement: (i) the decree establishing the Program Coordination Unit (PCU) will be published; (ii) the PCU’s core staff will be officially appointed; (iii) the management firm will be selected (see paragraph 3.3); and (iv) an agreement will be signed between the Município of Recife and URB RECIFE, delegating program execution, on terms satisfactory to the Bank (see paragraph 3.1).					
Special contractual execution conditions precedent to the start of works in Component I: (i) formal agreements will be signed between URB RECIFE and the departments involved in the execution of program activities, to ensure support for the execution of actions under their responsibility (see paragraph 3.5); (ii) in the cases of works involving the involuntary resettlement of families, the borrower will provide evidence, to the Bank’s satisfaction, that the families affected by the works under this component will be resettled in compliance with the conditions established in the Resettlement Plan, in accordance with the Bank’s Operational Policy on Involuntary Resettlement (OP-710, see paragraph 3.8); and (iii) the agreement between the borrower, the Urban Sanitation and Maintenance Company (EMLURB), and the Recife Urban Services Company (CSURB) for maintenance of the works under their responsibility will have been signed and entered into effect on terms satisfactory to the Bank.					
Exceptions to Bank policies: None.					
Project consistent with country strategy:					
		Yes [X]	No []		
Project qualifies as:		SEQ []	PTI []	Sector []	Geographic [] Headcount []

* The credit fee and inspection and supervision fee will be established periodically by the Board of Executive Directors as part of its review of the Bank's lending charges, in accordance with the applicable provisions of the Bank's policy on lending rate methodology for Ordinary Capital loans. In no case will the credit fee exceed 0.75% or the inspection and supervision fee exceed, in a given six-month period, the amount that would result from applying 1% to the loan amount divided by the number of six-month periods included in the original disbursement period.

** The individual operations approved under the PROCIDADES lending facility (document PR-3086-4) are financed with resources from the Single Currency Facility of the Bank's Ordinary Capital, with the option of converting disbursements and outstanding loan balances under the Local Currency Facility (LCF), in accordance with the terms previously approved by the Board of Executive Directors pursuant to Resolution DE-112/06, rather than the terms of the Flexible Financing Facility (document FN-655-1), established subsequently. As with a global credit program, the Bank, in discussions with the country authorities of Brazil, has developed a design for individual operations under the facility that allows the terms and conditions for disbursements in local currency to be standardized for all participating municípios (see document PR-3086-4, paragraph 5.17).

I. DESCRIPTION AND RESULTS MONITORING

A. Background, problem addressed, rationale

- 1.1 **The município.** Recife is the capital of the State of Pernambuco and has a resident urban population of 1.5 million. Greater Recife, encompassing 14 cities, is Brazil's fifth largest metropolitan region by size, and the largest in the Northeast region, with an estimated population of 3.7 million. The city is the state's main economic hub, accommodating 41.7% of its population, and producing one third of its total gross domestic product (GDP). Recife stands out as an international tourism, commercial, and cultural hub, owing to its historical heritage and its coastal attractions. It is also regional center as a nucleus of government operations, the tertiary sector, and specialized services.
- 1.2 The economy of Recife displays sharp contrasts. The city is one of Brazil's leading business centers, with highly developed economic sectors, including the hospital, construction, and technology¹ and logistics industries. It also has an airport and two international seaports. Nonetheless, the Município of Recife has an unemployment rate of 20.4%,² one of the highest among Brazil's metropolitan areas, nurturing the growth of informal activities, street commerce,³ and fear of crime. This explains why the município has a municipal human development index (HDI-M) of 0.797,⁴ which is considered mediocre and, although above the national average (0.699), places it fifteenth among Brazil's 27 state capitals.⁵
- 1.3 The city's urban infrastructure is generally good, and the coverage of several urban services has improved significantly. For example, access to drinking water expanded from 86% to 93% in the município between 2002 and 2005, while the coverage of garbage collection service increased from 82% to 96%.
- 1.4 **Principal urban problems: downtown Recife.** The city suffers from several ills typical of mature urban areas, such as the deterioration of certain downtown areas caused by shifting urban functions and relocation of the city's economic and residential centers. Downtown Recife, consisting of the boroughs (bairros) of Recife, Santo Antônio and São José, was settled in the colonial era along the banks of the Capibaribe River and on the edges of its mangrove swamps. Over the last three decades, these neighborhoods have steadily lost economic vigor, and their resident population has shrunk as new residential zones have expanded and new urban subcenters have emerged. This decline has created a paradox, specifically in the boroughs of Santo Antônio and São José: the poorest people are forced to

¹ Porto Digital is one of Brazil's largest technology parks, employing over 3,000 people and representing 3.5% of the state's economic activity.

² Inter-Union Department of Statistics and Socioeconomic Studies (DIEESE), 2009.

³ The Municipal Government of Recife estimates that there are currently some 8,000 street sellers in the município, 6,000 of them registered (Municipal Government of Recife).

⁴ United Nations Development Programme (UNDP), 2000.

⁵ In terms of HDI-M levels in the state of Pernambuco, Recife has dropped from first to third place in the state, behind the municípios of Fernando do Noronha and Paulista.

migrate to the outskirts of the city in search of cheaper homes, while the core areas retain a broad group of abandoned properties in a state of decay, offering major potential for occupation for housing, services, and commerce. The deterioration is particularly serious in areas around Avenida Guararapes, where 19% of properties are vacant, and Rua Imperial, where 15% of properties also stand empty. Both areas show a loss of economic and social vitality, with large unused buildings, run-down public spaces, declining irregular commerce, and haphazard informal activities. The two boroughs of São José and Santo Antônio also contain unregulated settlements with a total of 1,664 families living in at-risk areas or in conditions of urban overcrowding.

- 1.5 Personal safety is also an issue in Recife, which has one of the highest homicide rates⁶ of all Brazilian capital cities. Levels of violence in the Santo Antônio and São José neighborhoods, in particular, are starting to worry the authorities and the population at large. Acts of violence in those areas generally occur at night, exploiting the lack of a municipal police (Guarda Municipal) presence in the area. Insecurity is also exacerbated in these neighborhoods by the deterioration and abandonment of the surrounding area and the lack of alternative programs for young people and actions to prevent the circulation and use of drugs in the area.
- 1.6 **Institutional aspects.** The Municipal Government of Recife (known by its Portuguese-language acronym, PMR) has experience executing projects with multilateral financing,⁷ and the experience gained by Empresa de Urbanização do Recife [Recife Urban Development Corporation] (URB RECIFE), in particular, in executing these externally funded programs, is especially relevant for this program. The Bank's institutional diagnostic assessment determined that URB RECIFE possesses sufficient project delivery capacity, although strengthening of its staff is required this operation. A management firm will be hired to support it in that regard.
- 1.7 A number of institutional weaknesses have also been identified in two municipal departments relevant to this operation. The first is the Human Rights and Citizen Security Department (SDHSC), created in 2005 to coordinate intersector aspects of violence prevention and to develop alternative public policies in coordination with the National Public Safety System, working with civil society through strategic partnerships. This department has a small staff and suffers from technical weaknesses, including a lack of procedures and systems to generate reliable

⁶ The rate is 63 homicides per 100,000 inhabitants (official data from the State of Pernambuco Social Defense Department, 2008).

⁷ These projects include: the Bank's National Tourism Development Program (PRODETUR), Monumenta, and Habitar Brasil programs, the Capibaribe Melhor program funded by the World Bank, and others. The Monumenta program has already financed a number of urban improvements in the borough of Recife, near the target area of this program. The Municipal Government of Recife has also implemented the Tax Modernization Program (PMAT), and to give continuity to this it signed a contract in June 2004 with the federal savings bank, Caixa Econômica Federal (CEF), to promote municipal modernization, as part of the National Program to Support Administrative and Fiscal Management of Brazilian Municípios (PNAFM).

- information for decision-making on security and violence prevention. These problems will be addressed by the program's institutional strengthening component, which includes technical assistance to consolidate the department's information systems and thus make it easier to monitor and track the issues within its purview.
- 1.8 The other agency that requires strengthening is the Municipal Science, Technology and Economic Development Department (SCTDE), whose activities include developing initiatives to promote economic development⁸ and creating jobs for the city's neediest population groups. Nonetheless, these activities do not yet have an effective methodology either for an integrated approach or for monitoring and measurement of results. Thus far, they also have not been implemented in the program's target areas, and this is now a priority particularly in view of the socioeconomic needs of the respective populations.
- 1.9 **Strategy of the Município of Recife.** Concerned at the deterioration of the urban spaces representing Recife's cultural and historical heritage, and motivated by the need to invigorate the city's subcenters both economically and in urban development terms, the PMR has developed the Integrated Downtown Urban Conservation Project, Phase I, which identified 11 integrated rehabilitation perimeters called "PRIs" in the município, including this program's target areas in the heart of the city. Given their strategic importance in the city's geographic space, these areas were assigned priority for attention for their potential positive effects on the urban environment, and particularly for their proximity to the historical and monumental center of the Borough of Recife.
- 1.10 The Municipal Master Plan, approved in 2008, also envisages a number of actions for the downtown area and four special social interest zones (known by their Portuguese-language acronym, ZEIS). These include: (i) promoting tourism, recreation, and business activities; (ii) providing incentives for partnerships between private enterprise and the public authorities; (iii) promoting accessibility by restoring sidewalks and public spaces; (iv) refurbishing vacant or underused properties; (v) encouraging residential use, particularly in the form of low-income housing; and (vi) relocating families living in at-risk or unbuilt areas.
- 1.11 The PRI for the proposed areas includes the rehabilitation of buildings and improvement of public spaces and facilities. On Avenida Guararapes in the downtown area, it identified potential for developing commerce, services, and education activities, along with public facilities serving the whole metropolitan area that could be located in large, currently unoccupied buildings.
- 1.12 **Complementary actions in the central areas.** In compliance with the planning directives mentioned above, the PMR planned a set of actions and complementary works in the program areas. These include: (i) the Caminhos do Recife program, involving an upgrading of urban spaces around the Cinco Puntas Fort and the São José market (financed by PRODETUR); and (ii) the World Bank-funded

⁸ These include Banco do Povo, Empreender Mais Recife, and employment promotion centers.

Capibaribe Melhor program, which aims to resite makeshift dwellings along the banks of the Capibaribe river.

- 1.13 **Program strategy.** The present program will support the PMR in implementing the priorities identified in the downtown PRIs, particularly in terms of upgrading public spaces, solving housing problems for the population requiring resettlement, and providing incentives for the private sector to build new homes and refurbish existing ones. The program will also promote actions to diversify economic activities among low-income inhabitants, supported by violence prevention measures. The program will be supplemented by federally-funded investments in the housing sector, which will form part of the counterpart of this operation.
- 1.14 **Country strategy and GCI-9.** This operation is aligned with the Bank's country strategy with Brazil, 2012-2014 (document GN-2662-1), inasmuch as it aims to improve the urban habitat giving priority to the poorest areas, and to increase capacities for urban management and the provision of municipal services/infrastructure in medium-sized cities and metropolitan regions. The proposed program also satisfies the conditions, eligibility criteria, and investment sectors stipulated in the PROCIDADES lending facility.⁹ Furthermore, the project correlates with the GCI-9 lending program priority targets for poverty reduction and equity enhancement and for regional cooperation and integration (document AB-2764) in terms of the regional development goal for reduction in the number of homicides per 100,000 inhabitants; and the following outputs: (i) number of households with new or upgraded dwellings, (ii) municipal and other subnational governments supported; and (iii) cities benefited with citizen security projects.
- 1.15 **Rationale.** Given the importance of addressing municipal priorities in an integrated manner, the PMR has requested this loan operation from the Bank for improvements to restore its downtown areas.

B. Objectives, components, and costs

- 1.16 **Objectives.** The program's objective is to promote urban renewal in downtown Recife, with a view to enhancing the city's economic and territorial dynamic through urban improvements and economic and social development actions, thus improving the quality of life for the city's inhabitants. The program has the following components: (i) Urban and housing improvements; and (ii) institutional strengthening.
- 1.17 **Component I. Urban and housing improvements (US\$33.089 million).** This component seeks to promote urban development and environmental and social improvements in downtown Recife. The following actions and others will be financed in each of those target areas: (i) urban improvements and environmental remediation of streets, road surfaces, and recreational areas; (ii) urbanization of informal spaces and the construction of housing to resettle people living in the target

⁹ PROCIDADES (document PR-3086) is a lending facility to finance integrated urban development programs for Brazilian municípios, approved by the Bank's Board of Executive Directors on 11 October 2006.

areas; (iii) expansion of the social services network, including the construction and provision of basic furniture for priority facilities;¹⁰ (iv) the construction and provision of basic furniture and facilities for low-income commerce centers and the promotion of local economic activities; and (v) the contracting of urban development, architectural, and engineering studies and designs, as needed to execute the planned actions.

- 1.18 **Component II. Institutional strengthening — Complementary sector activities (US\$4.091 million).** This component will finance training and technical assistance for the key municipal agencies involved in program execution and those that undertake activities necessary for its success. The latter include: (i) support for URB RECIFE in strengthening its capacity to manage the program, by upgrading its physical premises and purchasing equipment, so that the PCU can function effectively; (ii) strengthening of the SCTDE to undertake productive activities, specifically through pilot initiatives to address informal commerce. The component will also finance technical assistance for this department, to consolidate a Local Economic Development Unit in the Rua Imperial zone, which will provide a personalized service and promote programs to support small-scale entrepreneurs. The programs in question will be supplied by the município and other public institutions, such as the Brazilian Microenterprise and Small Business Support Service (SEBRAE) and the National Industrial Training Service (SENAI), and others; and (iii) support for the SDHSC in strengthening its role in coordinating and directing actions on citizen security and violence prevention in the program areas. The following activities will be financed: (i) a socioeconomic diagnostic of the population in the program target areas, and preparation of citizen security action proposals; (ii) design of victimization surveys; (iii) creation of a municipal violence monitoring center;¹¹ (iv) creation of a social oversight mechanism and community dialogue roundtables on violence and dispute mediation; (v) support in terms of logistics and organization for municipal advisory boards and forums; and (vi) awareness-raising among civil servants and members of the municipal police.
- 1.19 **Program administration (US\$2.85 million).** The program will finance: (i) the hiring of a consulting firm for technical and environmental works supervision; (ii) the hiring of an external audit firm; (iii) monitoring and evaluation expenses;

¹⁰ The investments in question were prioritized taking account of the sector plans of the municipal Education, Health, and Social Assistance departments. They also considered the departments' institutional and financial capacity to bear the recurrent costs of the facilities to be financed, such as wages, materials, and maintenance.

¹¹ The monitoring center is an epidemiological surveillance system that validates information on violent and unintentional deaths and criminal acts of violence on a case-by-case basis with the institutions responsible for investigation, and analysis is done of those with greatest impact. Once processed, the records in question are deemed reliable information and are taken to an Analysis Committee where the local governance, justice, security and health authorities make decisions with a view to developing strategies and policies to prevent violence. This mechanism is currently a benchmark practice in several cities of the regions such as Bogotá, Medellín, Cali, Quito, and others.

and (iv) procurement and implementation of the program's computerized management system.

- 1.20 The component will also finance the following specific actions for inhabitants living in the program areas, to help prevent vulnerable and at-risk population groups from becoming involved in criminal activities: (i) the organization of cultural and sporting events, such as fairs, literary activities, cultural and digital inclusion workshops; and (ii) the organization of violence prevention activities in schools and at other education centers. All of these activities also seek to integrate the population into the job market.
- 1.21 **Costs.** The estimated total cost of the program is US\$40.03 million, 50% of which will be financed by the Bank with Ordinary Capital (OC) resources. The other 50% will be contributed by the Município of Recife. The following table summarizes the program costs and financing.

Table 1.1. Cost* and financing (US\$000s), exchange rate R\$2.00

Categories/components	IDB/OC	Local	Total	%
I. Urban and housing improvements	14,809	18,280	33,089	82.7%
II. Institutional strengthening	2,481	1,610	4,091	10.2%
Program administration	2,725	125	2,850	7.1%
Total	20,015	20,015	40,030	100%

* The finance charges, interest, credit fee, and inspection and supervision fee will be paid outside the program.

C. Key results indicators

- 1.22 The program's development impacts will be measured by means of the following indicators: (i) higher property values in the areas benefited by the program; (ii) higher commercial rents in the areas targeted directly by the program; and (iii) lower indicators of crime and violence in the program target areas (see Annex II).

II. FINANCING STRUCTURE AND MAIN RISKS

A. Financing instruments

- 2.1 This investment loan is governed by the PROCIDADES lending facility (document PR-3086).
- 2.2 **Disbursement schedule.** The projected execution period is four years, running from the effective date of the loan contract. The disbursement schedule is shown below.

Table 2.1. Disbursement Schedule (US\$ millions)

Source	Year 1	Year 2	Year 3	Year 4	Total
IDB	2.38	6.60	7.70	3.33	20.01
Município of Recife	5.70	8.58	4.40	1.34	20.01
Annual total	8.09	15.18	12.10	4.67	40.03
%	20.20	37.92	30.24	11.64	100

- 2.3 **Financial conditions.** The Município of Recife has requested use of the Bank’s Local Currency Facility (LCF). The proposed program will be implemented with resources drawn from the Single Currency Facility of the Bank’s Ordinary Capital in U.S. dollars, and would be subject to the new proposed Operational Framework for Lending in Local Currency (document GN-2365-6). In order to minimize exchange-rate risk, the Município of Recife will be entitled to convert disbursements and amounts owed into Brazilian reais, as provided in the LCF. In keeping with the PROCIDADES mechanism, this will meet the need identified by the Município of Recife to develop a public borrowing strategy with increasing local currency components, using resources drawn from the Single Currency Facility of the Bank’s Ordinary Capital.

B. Environmental and social safeguard risks

- 2.4 In compliance with the Bank’s Environment and Safeguards Compliance Policy (Operational Policy OP-703), an environmental assessment¹² of the program was prepared that identified the impact control and environmental mitigation and compensation measures needed to secure the program’s expected benefits. The results of the environmental assessment show that the program will not generate significant adverse environmental impacts, but will have a few minor impacts in the short term, arising from changes in the physical and socioeconomic environment, such as: (i) expropriation of properties for resettlement; (ii) alteration of traffic flows during works execution; and (iii) creation of noise, dust, and air pollution in areas around the works.
- 2.5 **Resettlement issues.** The program involves resettlement of the Coelhos and Villa Brasil communities—two irregular settlements located along the banks of the Capibaribe River, comprising a total of 1,296 families.¹³ It also involves housing improvement, urban development, and titling of homes belonging to 83 families in the João Paulo II community. Two housing complexes will be built to resettle the Coelhos and Vila Brasil communities, providing a total of 868 homes in areas close to the city center. The remaining population (345 families) will be accommodated in refurbished housing in the downtown area, supported by an assisted compensation program. To organize the intervention process, a complete resettlement plan was formulated in accordance with the requirements of the Bank’s

¹² Also known in Portuguese as the “relatório de avaliação ambiental” (RAA).

¹³ The Coelhos community, with 633 resident families, is on the right bank of the river Capibaribe; the Vila Brasil community, with 580 families, is on the left bank.

operational policy on Involuntary Resettlement (OP-710) and the housing policy of the city of Recife. This plan contains service guidelines, ensuring cost-free housing solutions to all families registered by the program; it also establishes a participation mechanism and proposes rehabilitation and social support programs to ensure the social and environmental sustainability of the new housing complexes.

- 2.6 In view of these features, the program has been classified as Category “B” under Operational Policy OP-703. The program was reviewed and approved on 22 March 2009 (ESR-12-09). The environmental and social management report (ESMR) for this operation was reviewed and approved by the Environmental Safeguards Unit (VPS/ESG) ([see required electronic link 3](#)).

C. Financial position of the Município of Recife

- 2.7 Financial and balance sheet analysis based on the accounts for 2006-2010, together with financial projections for the next 10 years, showed that the Município of Recife will be able to assume the loan with the Bank and contribute the necessary counterpart funds to conduct the program.
- 2.8 The Fiscal Responsibility Law (LRF) requires a number of financial indicators to be satisfied as a criterion for a município’s eligibility for external borrowing and to obtain the Brazilian Treasury guarantee. For that purpose, an analysis was made for the period 2006-2010, which, as shown in Table 2.2, confirms that the Município of Recife satisfies the established thresholds in all of the indicators analyzed.

Table 2.2. Indicators of the Fiscal Responsibility Law (%)

Indicators	Threshold	2006	2007	2008	2009	2010
Payroll expenses/net current income (NCI)	60	42.18	43.31	44.80	41.80	46.32
Net consolidated debt/NCI	120	21.88	31.46	27.82	24.90	25.01
Total guarantees	22	0	0	0	0	0
Domestic and external credit operations	16	2.24	0.59	0.11	0.31	1.04

D. Other key issues and risks

- 2.9 **Economic analysis.** A socioeconomic cost-benefit analysis was done, comparing benefits and costs in conditions with and without the program. The analysis considered a four-year period for program implementation and 20 years for the generation of benefits ([see optional electronic link 2](#)).
- 2.10 The cost calculation took overall account of the incremental costs of urban improvement, investment in social facilities, housing improvements and actions to upgrade the production and security environment. The projections also included maintenance costs.

- 2.11 The estimation of benefits assumed that program implementation would boost economic and productive activity, as reflected in the GDP produced in the program target area. The program target area includes the boroughs of São José and Santo Antônio.¹⁴ To measure the annual benefits, GDP growth projections were made for the target area with and without the program actions; the annual value of the difference between the two conditions represents the surplus resulting from the program's impact.
- 2.12 The results of the analysis show that the program is economically viable, with a capacity for generating positive benefits of R\$84.8 million in net present value terms, a benefit/cost ratio of 1.3, and an economic internal rate of return (EIRR) of 15.8%. Table 2.3 displays the general results obtained.

Table 2.3. Results of the Cost-benefit Analysis

Discrimination	Present value (R\$ millions)				EIRR (%)	B/C
	Benefit	Investment	Operation and maintenance	Net benefit		
Program	84.8	61.0	3.8	24.6	15.8	1.3

- 2.13 A sensitivity analysis of the program was also done by simulating changes in the expected benefits and costs incurred. The simulations entailed varying the values of estimated parameters (the difference between the increase in land values and the increase in investment costs). The projects admit cost increases of up to 30.9% and benefit reductions of 23.6%.
- 2.14 **Institutional capacity analysis.** The analysis using the Project Risk Assessment Tool (PRAT) rated program risk as moderate-high. The main implementation risk stems from the technical weaknesses of Municipal Government of Recife staff. To address this, a management firm will be hired to support the Program Coordination Unit in technical and administrative/financial aspects of the operation.

III. IMPLEMENTATION AND MANAGEMENT PLAN

A. Implementation mechanism

- 3.1 The borrower will be the Município of Recife. The Federative Republic of Brazil will guarantee the borrower's financial obligations under this operation. Empresa de Urbanização do Recife [Recife Urban Development Corporation] (URB RECIFE) will act as executing agency and a Program Coordination Unit (PCU) will be established within it by regulatory act. **As a special condition precedent to the first disbursement, an agreement will be signed between the Município of**

¹⁴ Data on Municipal Government of Recife tax revenue and GDP (Brazilian Institute of Geography and Statistics (IBGE), 2006). As economic output in the program target area is concentrated in the commerce and services sector, GDP was estimated for these sectors.

Recife and URB RECIFE, delegating responsibility for program execution, on terms satisfactory to the Bank.

- 3.2 The PCU will have core staff consisting of a general coordinator, technical director and a secretary. It will also have five coordination advisers for the following areas: (i) urban development; (ii) engineering; (iii) social issues; (iv) institutional development; and (v) administrative/financial issues. In addition, the core team will have two advisers, one for legal issues and another for bidding processes. The PCU personnel will be (i) technical staff of the Municipal Government of Recife (PMR); (ii) technical staff of other federal agencies; or (iii) engaged as consultants. The PCU will receive support from the coordination units or relevant sectors of URB RECIFE to supervise program works, and its Standing Bidding Committee to conduct bidding processes. The Standing Bidding Committee will receive training from the Bank on its policies and procedures.
- 3.3 The PCU will be assisted by a management firm in various aspects of program execution, including issues relating to planning, works, the environment, and administrative/accounting matters. **As special conditions precedent to the first disbursement: (i) the decree establishing the PCU will be published; (ii) the PCU's core staff will be officially appointed; (iii) the management firm will be selected.**
- 3.4 The PCU will: (i) coordinate and execute the various actions and interventions; (ii) promote communication and integration between the entities involved in the program; (iii) act as the sole interlocutor between the PMR and the Bank; and (iv) conduct the program's financial and accounting management. The PCU's main functions include the following: (i) planning of program investments and budgetary coordination with the corresponding departments; (ii) evaluation of final designs for the program's works; (iii) development of the management and accounting systems needed for physical/financial monitoring of the program. (iv) physical/financial control and preparation of the respective status reports; (v) preparation and support of bidding processes for works, and procurement of goods and services; (vi) coordination and supervision of any necessary expropriation plans; (vii) support for works supervision and inspection; (viii) coordination and supervision of social and environmental matters; (ix) oversight of accounting and record-keeping, submission of disbursement requests, and delivery of accounts; (x) monitoring and coordination of fulfillment of the contractual clauses contained in the loan contract; (xi) monitoring and evaluation of the results, targets, and indicators defined in the Results Matrix; (xii) preparation of annual work plans (AWPs); (xiii) preparation of terms of reference for contracting of individual consultants and consulting firms; (xiv) preparation of all technical and administrative documentation relevant to bidding and contracting processes; and (xv) preparation of other reports as requested by the Bank.
- 3.5 The following departments will participate actively in program implementation: Department of Oversight, Urban Development, and Works (SCDUO); Housing (SEHAB); Social Assistance (SAS); Health (SS); Education, Sports, and Recreation

- (SEEL); Science, Technology, and Economic Development (SCTDE); and Human Rights and Citizen Security (SDHSC), as well as the urban sanitation and maintenance company, EMLURB. Each of these entities will appoint a staff member from its payroll to coordinate the actions for which it is responsible, in agreement with the PCU coordinator general. As a special execution condition precedent to the start of works in Component I, formal agreements will be signed between URB RECIFE and the departments involved in the execution of program activities, to ensure support for the execution of actions under their responsibility.
- 3.6 To improve sector coordination in implementing this operation, a program Institutional Coordination Committee will be formed, with the PCU general coordinator serving as executive secretary. The committee will comprise technical staff appointed by the departments involved in execution of the operation (see paragraph 3.5). It will meet regularly each month, and as necessary to make decisions on important issues relating to the operation. The committee will also be responsible for evaluating and contributing to the preparation of annual work plans and the operation's status reports.
- 3.7 **Component execution arrangements.** The PCU will be responsible for the coordination and general supervision of program execution; and the general coordinator will serve as a link between the PCU and each of the entities involved in implementing their respective components.
- 3.8 Component I will be executed by the PCU, in close coordination with SCDUO, SEHAB, SAS, SS, SEEL, and SCTDE. These departments will (i) help prepare projects and procure equipment within their sectors; and (ii) will support the implementation of those projects, to guarantee future operation and maintenance at appropriate levels. EMLURB and the Recife Urban Services Company (CSURB) will be responsible for the maintenance of the program works in their respective areas of jurisdiction as provided by law. As a special execution condition precedent to the start of works in Component I, the agreement between the Município of Recife and EMLURB for maintenance of the works under its responsibility will have been signed and entered into effect on terms satisfactory to the Bank. In addition, in the cases of works involving the involuntary resettlement of families, the borrower will provide evidence, to the Bank's satisfaction, that the families affected by the works under this component will be resettled in compliance with the conditions established in the Resettlement Plan, in accordance with the Bank's Operational Policy on Involuntary Resettlement (OP-710).
- 3.9 The institutional strengthening component will be implemented by the PCU, which will coordinate specifically with the SDHSC for the citizen security and violence prevention components. The SDHSC will also coordinate and organize interagency coordination tasks with other PMR departments, on issues that require an integrated approach. The PCU will also collaborate specifically with the SCTDE on local economic development actions.

- 3.10 **Procurement.** Works, goods, and services will be procured in accordance with the “Policies for the procurement of goods and works financed by the Inter-American Development Bank” and “Policies for the selection and contracting of consultants financed by the Inter-American Development Bank” (documents GN-2349-9 and GN-2350-9). Procurement processes for works, goods and services, and consulting services will be subject to ex ante review, as will the first disbursement process, so that the Bank can guide and ensure the PMR’s capacity in this type of procedure. After the first year of execution, the Bank may, at its own discretion, adopt an ex post review arrangement for the remainder of program execution (see Annex III).
- 3.11 **Recognition of expenditures.** The PMR has requested recognition as program local counterpart by the Bank of up to US\$10 million in expenditures incurred within 18 months prior to approval of the operation by the Bank’s Board of Executive Directors for the procurement of works, designs, and consulting services. These procurements will follow the procedures established in local legislation, and will be recognized to the extent that they comply with the Bank policies established in documents GN-2349-9 and GN-2350-9.¹⁵
- 3.12 **Advance of funds.** Advances of funds will be requested by the PMR through the PCU every six months or as needed for the project, according to a financial plan accompanying each request. The executing agency will deliver six-monthly reports to the Bank on use of the advance of funds, within 60 calendar days after the close of each six-month period.
- 3.13 **Audits.** During execution, the PCU will deliver the audited financial statements for the program on an annual basis, within 120 days after the end of each fiscal year. The program closeout audit reports will be delivered within 120 days after the last disbursement.

B. Monitoring and evaluation arrangements

- 3.14 **Monitoring system.** To ensure the effective monitoring of actions throughout program execution, the PCU will institute a management and financial/accounting oversight system, compatible with the Bank’s systems, which will also allow monitoring of fulfillment of the program outcome and output indicators. These are specified in the Results Matrix (see Annex II) and include: (i) the tracking of physical progress and meeting of program annual targets; (ii) evaluation of the outcomes of these actions and projects; and (iii) program efficiency and effectiveness.

¹⁵ The procedures described in these policies apply to all procurements of goods and works financed, in whole or in part, with the loan proceeds. The borrower may adopt other procedures for the procurement of goods and works not financed from a loan. In such cases, the Bank shall be satisfied that the procedures to be used satisfy the Borrower’s obligation to ensure that the project is carried out diligently and efficiently, and that the goods and works to be procured: (i) are of satisfactory quality and are compatible with the balance of the project; (ii) will be delivered or completed in timely fashion; and (iii) are priced so as not to affect adversely the economic and financial viability of the project.

- 3.15 **Midterm and final reviews.** The PCU will prepare and deliver a midterm review report to the Bank, within 90 days after the date on which 50% of the loan proceeds have been disbursed, or when 30 months of execution have elapsed, whichever occurs first. It will also prepare and deliver to the Bank a final evaluation report that will serve as an input for the project completion report (PCR), within 90 days after the date on which 90% of the loan proceeds have been disbursed. These reports will include: (i) the results of financial execution by component; (ii) outcome and output targets met, and progress toward expected impacts, according to the indicators contained in the Results Matrix (see Annex I); (iii) the degree to which works environmental requirements and specifications have been met, as established in the environmental and social management report (ESMR) and the respective permits; (iv) the degree to which operation and maintenance tasks have been conducted on completed works; (v) a summary of the most important socioenvironmental impacts; (vi) the degree to which contractual commitments have been met; and (vii) a summary of the findings of all audits performed during program execution. Once accepted by the Bank, these two evaluation reports will be published on the PMR website. These evaluations will be performed by consulting firms commissioned by the PCU and financed with the loan proceeds.
- 3.16 **Ex post evaluation.** The program includes an ex post evaluation to measure the impact of the program activities on the four key questions asked by the evaluation: Have the transformations brought about by the comprehensive interventions resulted in (i) higher property values in the area targeted directly by the program; (ii) higher revenue intake from the real estate transfer tax (ITBI); (iii) higher commercial rents in the areas targeted directly by the program; and (iv) less crime and violence in the program target areas? The ex post evaluation will employ the reflexive methodology. The main technical reason for choosing this methodology is that a counterfactual cannot be constructed to evaluate the intervention overall, given the scope, distribution of interventions, and unique features of the various areas within the municipality, so a comparison group cannot be constructed. Nor would a statistical comparison with another city or urban center have statistical power. Moreover, the reflexive methodology is widely used in interventions of this nature, and provides feedback for the entire urban intervention process. The information for the baseline will be updated at program start, such that the trajectory of the indicators prior to the intervention can be observed, making it possible to assess whether the intervention results in an inflection point in the indicators.

C. Significant activities post approval

- 3.17 The PMR will execute the following works in the first year of program implementation: (i) the 2,300 square-meter market annex building, to house some of the informal commercial activity; (ii) a municipal early childhood learning center (CEMEI), and (iii) a family health center (PSF). Counterpart works and financing activities for all resettlement housing units. These works jointly account for 18% of the program cost. During the first year, the PMR will also have to prepare projects

to implement the remaining program works, such as urban renewal and the other social facilities.

Development Effectiveness Matrix			
Summary			
I. Strategic Alignment			
1. IDB Strategic Development Objectives	Aligned		
Lending Program	The intervention contributes to the lending program for (i) poverty reduction and equity enhancement, (ii) climate change initiatives, renewable energy and environmental sustainability, and (iii) regional cooperation and integration.		
Regional Development Goals	The intervention contributes to (i) paved road coverage (Km/Km ²), and (ii) Homicides per 100,000 inhabitants.		
Bank Output Contribution (as defined in Results Framework of IDB-9)	The intervention contributes to the Bank’s outputs: (i) Km of inter-urban roads build or maintained/upgraded, and (ii) Number of households with new or upgraded dwellings.		
2. Country Strategy Development Objectives	Aligned		
Country Strategy Results Matrix	GN-2662-1	Improve the urban habitat giving priority to the poorest areas.	
Country Program Results Matrix	GN-2661-4	The project is included in 2012 Country Program Document.	
Relevance of this project to country development challenges (If not aligned to country strategy or country program)			
II. Development Outcomes - Evaluability	Highly Evaluable	Weight	Maximum Score
	8.1		10
3. Evidence-based Assessment & Solution	8.6	25%	10
4. Ex ante Economic Analysis	10.0	25%	10
5. Monitoring and Evaluation	6.5	25%	10
6. Risks & Mitigation Monitoring Matrix	7.5	25%	10
Overall risks rate = magnitude of risks*likelihood		Medium - High	
Environmental & social risk classification		B	
III. IDB’s Role - Additionality			
The project relies on the use of country systems (VPC/PDP criteria)	Yes	Financial Management: Treasury, Budget, Accounting and Reporting, and External Control. Procurement: Shopping Method and Contracting Individual Consultant.	
The project uses another country system different from the ones above for implementing the program			
The IDB’s involvement promotes improvements of the intended beneficiaries and/or public sector entity in the following dimensions:			
Gender Equality			
Labor	Yes	The intervention will support the strengthening of the technical and operative capacities of the Ministries involved; among them is the Ministry of Economic Development.	
Environment			
Additional (to project preparation) technical assistance was provided to the public sector entity prior to approval to increase the likelihood of success of the project			
The ex-post impact evaluation of the project will produce evidence to close knowledge gaps in the sector that were identified in the project document and/or in the evaluation plan			

The program supports the Government of Brazil to improve the quality of life for residents of the Municipality of Recife, especially those residing in inner city areas. This will be done through the implementation of integrated urban development projects, interventions in economic and social development, and action to strengthen municipal management to increase economic and territorial dynamics of the city. Urban development projects include urban improvements, environmental and social conditions in the central areas of Recife through interventions in: (i) urban improvements and environmental restoration of streets, roads, parks and sports and recreation, (ii) urbanization informal spaces and construction of houses for resettlement of population, (iii) expanding the network of social services, and (iv) the construction and provision of basic equipment and furniture popular shopping centers and promotion of local economic activities.

The project has a definition of the problem based on empirical evidence, in addition, identifies the main factors contributing to this problem with their corresponding dimensions. The objectives and rationale of the intervention are clear. The project results matrix includes outputs and outcomes indicators that will enable appropriate monitoring and evaluation. The project has a cost benefit analysis ex-ante. In terms of the evaluation, a Before and After methodology is considered. The project has a risk matrix that identifies potential difficulties in implementation, as well as mitigation measures.

RESULTS MATRIX

Program general objective:	The program's objective is to promote urban renewal in downtown Recife through urban improvements and local actions to enhance the economic and social dynamic, thus improving the quality of life for the city's inhabitants.			
Outcomes	Unit of measure	Baseline/year	Target (end of year 4)	Source/means of verification
Outcome 1. Higher property values in the area targeted directly by the program; transformations brought about by the interventions				
Value, in real terms, of real estate in the area targeted directly by the program (the boroughs of Santo Antônio and São José) after project year 4.	R\$/m ²	R\$500/m ² (2009)	R\$575/m ² (project year 4)	Source: information gathered by PCU.
Outcome 2. Higher commercial rents in the areas targeted directly by the program				
Real value of commercial rents in area of Avenida Guararapes.	R\$/m ²	R\$7.28/m ² (2009)	R\$9.56/m ²	Source: information gathered by PCU.
Outcome 3. Less crime and violence in the program target areas				
Occurrence of intentional lethal violent crime (ILVC) per 100,000 inhabitants	Occurrences/100,000 inhabitants	ILVC: 119/100,000 inhabitants (2008)	ILVC: 90/100,000 inhabitants	Source: information gathered by the Municipal Human Rights and Citizen Security Department (SDHSC), with data from the Department of Social Defense of the State (SDS).

Outputs	Unit of measure	Baseline 2009*	Year 1	Year 2	Year 3	Year 4	Target	Comments
COMPONENT I. URBAN AND HOUSING IMPROVEMENTS								
Improvements to Praça Sérgio Loreto [Sérgio Loreto Square].	m²	0	0	110	0	0	110	Source: Program annual report, PCU, with data from the Department of Oversight, Urban Development, and Works (SCDUO).
Improvements to Praça da Educação (Rua José Enrique Vanderley).	m²	0	0	0	90	0	90	Source: Program annual report, PCU.
Improvements to Praça Sebo [Sebo Square].	m²	0	0	100	100	0	200	Source: Program annual report, PCU, with data from SCDUO.
Restoration of Rua Imperial completed.	km	0	0	1 km	1 km	0	2 km	Source: Program annual report, PCU, with data from SCDUO.
Restoration of Rua Dantas Barreto completed.	km	0	0	0	1.6 km	0	1.6 km	Source: Program annual report, PCU, with data from SCDUO.
Restoration of Avenida Central completed.	km	0	0	2 km	2 km	0	4 km	Source: Program annual report, PCU, with data from SCDUO.
Restoration of Avenida Concordia and Floriano Peixoto completed.	km	0	0	0	2 km	0	2 km	Source: Program annual report, PCU, with data from SCDUO.
Housing units built at Praça Sérgio Loreto.	Housing units	0	40	60	0	0	100	Source: Program annual report, PCU, with data from the Municipal Housing Department (SEHAB).
Housing units built in the Coelhos community.	Housing units	0	154	230	0	0	384	Source: Program annual report, PCU, with data from SEHAB.
Housing units built in Ave. Imperial.	Housing units	0	40	60	0	0	100	Source: Program annual report, PCU, with data from SEHAB.
Housing units implemented in the Vila Brasil community.	Housing units	0	160	160	80	0	400	Source: Program annual report, PCU, with data from SEHAB.
Low-income shopping center built and operating.	Shopping center	0	1	0	0	0	1	Source: Program annual report, PCU, with data from CSDUP and SEHAB.

Outputs	Unit of measure	Baseline 2009*	Year 1	Year 2	Year 3	Year 4	Target	Comments
New early childhood education centers (CEMEIs) built and operating at Praça Sérgio Loreto, in the Espólio Estevinho community and in the Vila Brasil community (each serving at least 120 pupils).	CEMEIs	0	1	1	1	0	3	Source: Program annual report, PCU, with data from the Municipal Education, Sports, and Recreation Department (SEEL).
New family health centers (PSFs) built and operating in the Espólio Estevinho and Imperial communities (each serving an average of 3,500 people per year).	PSFs	0	1	1	0	0	2	Source: Program annual report, PCU, with data from the Ministry of Health (SS).
Community social center opened and operating (serving at least 100 people per month).	Community social center	0	0	0	1	0	1	Source: Program annual report, PCU, with data from the Municipal Social Assistance Department (SAS).
COMPONENT II. INSTITUTIONAL STRENGTHENING — COMPLEMENTARY SECTOR ACTIVITIES								
Physical restoration of the PCU in the URB RECIFE building	m²	0	70	0	0	0	70	Source: Program annual report, PCU, with data from the Urban Development Corporation (URB).
Local economic development unit built and operating in the Imperial neighborhood.	Development unit	0	0	1	0	0	1	Source: Program annual report, PCU, with data from the Municipal Science, Technology, and Economic Development Department (SCTDE).
Economic activities monitoring system implemented and operating in the SCTDE.	System	0	0	1	0	0	1	Source: Program annual report, PCU, with data from SCTDE.
60 Master carpenters and 150 assistant carpenters trained in furniture production.	Participants	0	0	20 master and 50 assistants trained	20 master and 50 assistants trained	20 master and 50 assistants trained	60 master and 150 assistants trained	Source: Program annual report, PCU, with data from SCTDE.
Victimization surveys.	Surveys	0	1	0	0	1	2	Source: Program annual report, PCU, with data from the Municipal Human Rights and Citizen Security Department (SDHSC).
Managers trained.	Participants	0	40	40	40	40	160	Source: Program annual report, PCU, with data from SDHSC.

Outputs	Unit of measure	Baseline 2009*	Year 1	Year 2	Year 3	Year 4	Target	Comments
Municipal police awareness-raising.	Participants	0	50	50	50	50	200	Source: Program annual report, PCU, with data from SDHSC.
Violence observatory operating (including website and other available data covering the whole territory of the Município of Recife).	Observatory	0	Website created	0	0	0	1 observatory 100% up and running	Source: Program annual report, PCU, with data from SDHSC.

* Baseline established as of 2009, which was the year of approval of the project profile.

FIDUCIARY AGREEMENTS AND REQUIREMENTS

Country: Brazil

Project number: BR-L1190

Executing agency: Empresa de Urbanização do Recife [Recife Urban Development Corporation] (URB RECIFE)

Prepared by: José Luis Vázquez (financial specialist) and Marília Santos (procurement specialist)

I. EXECUTIVE SUMMARY

The fiduciary assessment was conducted during preparation of the draft proposal for operation development (POD) for the project (CBR-4153/2009 including a project risk assessment tool (PRAT) analysis). Subsequently, for this annex, a desk review of the proposal and supplemental information provided by the Municipal Government of Recife (PMR) have been drawn on to determine a potential advance in project risk management (PRM), an action plan, and proposed financial agreements to be applied for project execution but which, nonetheless, need to be updated as a prelaunch workshop with the counterpart.

In addition, the fiduciary context of the country and the Município of Recife and, in particular, of URB RECIFE has been taken into account for the establishment of the fiduciary agreements, the principal points of which are summarized in the following paragraphs.

II. FIDUCIARY CONTEXT OF THE EXECUTING AGENCY

The borrower will be the Município of Recife. The guarantor will be the Federative Republic of Brazil. The executing agency will be the Município of Recife, acting through URB RECIFE.

URB will establish a program coordination unit (PCU) with core staff comprised of the program coordinator, who will be the liaison accountable to the Bank, a technical director, and a team of coordination advisors: (i) urban development; (ii) engineering (iii) social issues; (iv) institutional development; and (iv) administrative/financial, as well as two thematic advisors: one legal and one in procurement. The PCU structure and key staff profiles will be established in the program Operating Regulations.

III. FIDUCIARY RISK EVALUATION AND MITIGATION MEASURES

The PRAT concluded that the risk of the operation is moderate high. The main risk identified is the lack of qualified personnel for program execution. To mitigate this risk, a management firm will be engaged to support the PCU in technical areas and in general program administration. The program risk matrix shows medium risk levels in the following areas: (i) governance (referring to changes in the municipal government), which will be mitigated by formalizing the commitments made by the Município to the Bank and the federal government to implement the program in accordance with the agreements signed; (ii) fiduciary (a lack of experience with the Bank), which will be mitigated by engagement of the management firm; (iii) failure to observe timetables; (iv) lack of information systems integrated with PFR central systems; and (v) control environment (internal and external). As mentioned, once the operation is approved, it will be updated jointly with the executing agency using the PRM methodology. In this regard, a risk potentially requiring precautionary measures involves the macroeconomic environment. Price increases, especially in the construction industry, coupled with a decline in the dollar's purchasing power, could lead to financial imbalances and unsuccessful bidding processes. Therefore, as a mitigation measure, updated maintenance of the project cost and the respective budget adequacy will be continually monitored, thus allowing for timely corrective measures. At the same time, efforts will be made to incorporate the project into the municipal government's routines and processing flows related to budgeting, commitment circuits, expenditures, payments, record-keeping, and financial reporting. The Bank's supervision of these areas will be intensified, initially by means of annual supervision missions, which may be adjusted as the project advances and mitigation measures are implemented.

IV. CONSIDERATIONS FOR THE SPECIAL PROVISIONS OF THE CONTRACTS

- a. As conditions precedent to the first disbursement for the program: (i) the program coordination unit (PCU) will be officially established, and its core staff appointed (see paragraph 3.3); (ii) the management firm will be selected (see paragraph 3.3); (iii) the management and financial/accounting control system for the program will be selected (see paragraph 3.14); and (iv) an agreement will be signed between the Município of Recife and URB RECIFE, delegating responsibility for program execution, on terms satisfactory to the Bank.
- b. The Municipal Government of Recife will inform the Bank of the selected exchange rate modality before the contract is signed.
- c. The executing agency will deliver the project's annual financial statements, audited by an auditing firm acceptable to the Bank, within 120 days after the close of each fiscal year, beginning with the statements for the year when loan disbursements begin.
- d. The audits, which will be conducted in accordance with the Bank's current guidelines, will include a review, which may be by sampling, of applicable disbursement and procurement processes for that period. The auditors will also

perform interim inspections (with a cutoff of 30 June of each auditable year). The auditors will be engaged at least four months (31 August) prior the first year to be audited, and the executing agency will make arrangements to ensure compliance, if necessary through an additional selection process or processes.

V. AGREEMENTS AND REQUIREMENTS FOR PROCUREMENT EXECUTION

The fiduciary agreements and requirements for procurement establish the provisions applicable to the execution of all procurements under the project.

1. Procurement execution

- a. **Procurement of works, goods, and nonconsulting services:** The procurement of works, goods, and related services will be subject to the Bank's bidding policies and procedures, in accordance with document GN-2349-9. If the estimated cost of a works contract is US\$25 million or more, and the cost of a goods and services contract is US\$5 million or more, procurement will be subject to international competitive bidding (ICB) procedures. Works contracts and goods and services contracts with an estimated cost of less than US\$25 million and US\$5 million, respectively, will be subject to national competitive bidding (NCB) procedures. Works contracts and contracts for goods and services that are neither consulting services nor off-the-shelf goods, with an estimated cost of less than US\$500,000 and US\$100,000, respectively, may use the shopping method for procurement.

The Bank may also recognize the following procurement methods established in Law 10520 (the "Pregão Eletrônico" Electronic Reverse Auction Act) chargeable against the loan proceeds: (i) e-reverse auction, using Bank-approved systems for the procurement of off-the-shelf goods and services with an estimated cost of US\$5 million or less; (ii) price schedule for the procurement of off-the-shelf goods and services with an estimated cost of US\$5 million or less, provided registration has been previously accepted by the Bank; and (iii) live reverse auction for the procurement of off-the-shelf goods and services with an estimated cost of less than US\$100,000. The Bank may, at any time during program execution, cease to allow the use of one or more of the methods described in this paragraph.

- b. **Selection and contracting of consultants:** The selection and contracting of suitable consulting firms to be financed with loan proceeds will be subject to the Bank's policies and procedures, in accordance with document GN-2350-9. All consulting contracts for US\$200,000 equivalent or more will be subject to international publicity. In the case of consulting contracts for less than US\$1 million, the short list may comprise entirely national consultants.
- c. **Selection of individual consultants:** Individual consultants will be selected and contracted in accordance with section 5 of the "Policies for the Selection and Contracting of Consultants Financed by the Inter-American Development Bank" (document GN-2350-9).

- d. **Advance procurement/Retroactive financing:** The Bank may recognize up to US\$3 million equivalent against the counterpart for expenditures incurred for the preparation of eligible works and projects and consulting services for the operation. The procedures used in the selection and contracting of eligible expenditures must have followed the rules established in local legislation. Both the amount and the time limit for recognition of these expenditures are in compliance with Operational Policy OP-504, and with the guidelines of the Operations Policy Committee (OPC). Expenditures incurred after 9 April 2009, which is the date of approval of the project profile, will be recognized.

2. Table of threshold amounts (US\$000s)

Works			Goods ¹			Consulting	
International competitive bidding	National competitive bidding	Shopping	International competitive bidding	National competitive bidding	Shopping	International publicity consulting	Shortlist 100% national
≥ 25,000,000	< 25,000,000 ≥ 500,000	< 500,000	≥ 5,000,000	< 500,000 ≥ 100,000	< 100,000	> 200,000	< 1,000,000

3. Major procurement processes

The main procurements are presented in the program procurement plan, attached as Appendix I to this document.

4. Procurement supervision

The first two procurement processes of each modality conducted with loan proceeds, regardless of amount, will be subject to ex ante review by the Bank. Subsequently, all processes will be subject to ex post review, with the exception of direct contracting and single-source selection, and those exceeding the Bank's threshold set for Brazil for international competitive bidding.

5. Special provisions

The PCU will update the procurement plan at least every six months, or as required by the Bank to reflect actual project execution requirements and progress made.

6. Records and files

Program records and files must meet at least the following conditions:

- The files will contain original documentation, filed in chronological order and stamped and numbered consecutively.
- The files will be kept in a secure room used exclusively for that purpose, with restricted access.
- A record of the files will be kept.

¹ Includes nonconsulting services.

VI. FINANCIAL MANAGEMENT

1. Programming and budget

The **Special Management and Planning Department (SEGESP)** of the Município of Recife prepares the annual programming and budget for external and counterpart financing, based on requests submitted by the budgetary units (requesting units), to be supported by the PCU. The budget is managed under the budgetary and financial systems SPPA, SPOR (income plan register), and SPOD (expenditure register). The municipal government will need to fully incorporate the financial requirements into its routines according to the investment schedule in effect.

The Bank will reimburse eligible project expenditures in accordance with the investment activities and categories planned and executed for the project, and the municipal government will adjust its budget line items accordingly.

2. Accounting and information systems

The project will use the above-mentioned budgeting and financial systems (SPPA, SPOR, SPOD) and the SOFIN budget, financial, and asset system. The Municipal Department of Finance will support the PCU in adapting the budget and financial systems to the program's needs, such that project accounting records can be kept, and the required financial reports and statements, including preparation of disbursement requests and exchange rate monitoring, can be issued directly from the information systems. Accounting will be on a cash basis and compliant with international accounting standards, with which the Municipal Government of Recife is expected to be fully aligned by 2013. As part of the general conditions precedent, the executing agency will provide the Bank with evidence of the financial, accounting, and internal control systems for the project, including the specific account code to be used for the operation's financial and accounting management. It will also provide evidence of the adjustments made to the municipal government's systems, allowing the required financial reports for the project to be generated directly, or via additional integrated modules, stated in U.S. dollars and organized according to investment category and source of financing as envisaged in the project and in accordance with current Bank models.

3. Disbursements and cash flow

The project will use the available SOFIN modules to determine the availability of funds and monitor payments: (i) the budget module permits allocations to be established by source of funds; (ii) the financial programming module shows the six-monthly availability of financial balances to meet commitments; (iii) the commitment and liquidation module reports commitments to subsequently authorize recognition of expenditures; and (iv) the payments module permits authorized payments of recognized expenditures to be processed through electronic bank orders into the registered accounts of the beneficiaries. Accordingly, expenditures are compliant with the budget and financial execution process and will be reported in the SOFIN information system with data related to their formalization pursuant to the legal requirements for each stage: commitment, obligation, warrant and disbursement.

The program will operate with the Bank's disbursement modalities, chiefly advances of funds. Advances will be made according to the program's cash flow requirements, estimated by the executing agency in accordance with projected payments planned for commitments formalized with the Bank's knowledge (PRISM code, or equivalent), and consistent with the annual work plan and the procurement plan.

The PCU will submit the disbursement request to the Bank for the advance of funds (initial, full or partial renewal, or increase), together with the financial plan and the projected cash flow mentioned above, for the next 120 days. Justification will be provided for at least 80% of disbursements when the next request is submitted.

The PCU will submit the project's initial financial plan to the Bank, reflecting the disbursement schedule for the entire project, which will be updated annually or as necessary.

Supporting documentation for expenditures and payments will be subject to ex post review by the external auditors as part of the project's audited financial statements.

Prior to the first disbursement, the executing agency will provide the Bank with banking information (routing) to process disbursements. As a general condition precedent related to the project's financial, accounting, and internal control system, the executing agency will also inform the Bank of the proposed banking arrangements (for example: IDB; General account, municipal government = local counterpart; operating account – payments account).

4. Internal control and internal audit

The State Audit Office and the Attorney General's Office are responsible for oversight of municipal departments for the control and monitoring of activities.

For the general condition precedent mentioned above, the municipal government will provide detailed information regarding its formal system of internal control, identifying the municipal government division responsible, as applicable, including process flowcharts, parties involved, availability of manuals, process regulations, work plans, etc. At the same time, it will also state which specific mechanisms apply to the project. In this regard, the PCU will be required to include such control mechanisms in the Operating Regulations, contributing to their timely and satisfactory operation.

5. External control and reports

The municipal government reports to the local legislative council on a regular basis and is subject to review by the State Audit Office. These reviews, however, do not fully cover the project. Consequently, in order to deliver the project's financial statements to the Bank with a full external opinion, the Município of Recife will engage an independent auditing firm acceptable to the Bank at least four months prior the close of the first auditable year. The firm will be selected using a selection procedure and scope of work in accordance with the Bank's current rules and guidelines. The reports to be delivered to the Bank will be stated in U.S. dollars and will include the project's financial statements (cash flow and status of cumulative investments by category and financing source), notes to the statements, including reconciliation of amounts owed to the Bank and advance of funds statement, opinion on contractual compliance in terms of financial accounting, internal control system,

and review of disbursement process, and, as applicable, procurement processes during the year.

The audited financial statements will be delivered to the Bank on an annual basis within 120 days after the close of each year, beginning with the year in which loan disbursements commence. The auditors will also perform interim inspections (June of each year to be audited) and will provide the executing agency with a brief report listing any internal control recommendations. This review will also cover disbursement and procurement processes for the period, as applicable.

6. Financial supervision plan

Please see Annex 2, attached.

7. Execution mechanism

Given the execution mechanism described in the POD, the centralization of administrative, financial, and accounting execution arrangements through the PCU will be required. The PCU will be responsible for formulating the annual budget, both for the local counterpart and for the IDB contribution. The PCU will be the liaison to the Bank, and in charge of processing payments, managing disbursements, delivering financial reports to the Bank, and coordinating all activities with other participating agencies. As a condition precedent, the Município of Recife will provide evidence to the Bank that the PCU has been formally established, including detailed flowcharts on operational, administrative, accounting, financial, and internal control processes, as well as information on the parties involved. The corresponding requirements will be included in the project Operating Regulations.