

SIMULTANEOUS DISCLOSURE

DOCUMENT OF THE INTER-AMERICAN DEVELOPMENT BANK

## **COSTA RICA**

### **EDUCATION INFRASTRUCTURE CONSTRUCTION AND EQUIPMENT**

**(CR-L1053)**

### **LOAN PROPOSAL**

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## CONTENTS

### PROJECT SUMMARY

|      |   |    |
|------|---|----|
| I.   | DESCRIPTION AND RESULTS MONITORING .....                  | 1  |
| A.   | Background, problems to be addressed, and rationale ..... | 1  |
| B.   | Objectives, components, and cost .....                    | 7  |
| C.   | Key indicators in the results matrix .....                | 9  |
| II.  | FINANCING STRUCTURE AND RISKS .....                       | 9  |
| A.   | Financing instruments .....                               | 9  |
| B.   | Risks .....   | 10 |
| III. | IMPLEMENTATION AND ACTION PLAN .....                      | 11 |
| A.   | Summary of execution arrangements .....                   | 11 |
| B.   | Procurement .....   | 13 |
| C.   | Retroactive financing and auditing .....                  | 13 |
| D.   | Monitoring and evaluation .....                           | 13 |

| ANNEXES   |  |
|-----------|--|
| Annex I   | Summary Development Effectiveness Matrix (DEM) |
| Annex II  | Results matrix                                 |
| Annex III | Fiduciary agreements and requirements          |

| ELECTRONIC LINKS    |  |
|---------------------|--|
| <b>REQUIRED</b>     |  |
| 1.                  | Annual work plan<br><a href="http://idbdocs.iadb.org/wsdocs/getDocument.aspx?DOCNUM=37027704">http://idbdocs.iadb.org/wsdocs/getDocument.aspx?DOCNUM=37027704</a>  |
| 2.                  | Monitoring and evaluation arrangements<br><a href="http://idbdocs.iadb.org/wsdocs/getDocument.aspx?DOCNUM=37027708">http://idbdocs.iadb.org/wsdocs/getDocument.aspx?DOCNUM=37027708</a>  |
| 3.                  | Procurement plan<br><a href="http://idbdocs.iadb.org/wsdocs/getDocument.aspx?DOCNUM=37027703">http://idbdocs.iadb.org/wsdocs/getDocument.aspx?DOCNUM=37027703</a>  |
| 4.                  | Environmental and Social Management Report (ESMR)<br><a href="http://idbdocs.iadb.org/wsdocs/getDocument.aspx?DOCNUM=37027710">http://idbdocs.iadb.org/wsdocs/getDocument.aspx?DOCNUM=37027710</a>   |
| <b>OPTIONAL</b>     |  |
| 1.                  | Sector work index<br><a href="http://idbdocs.iadb.org/wsdocs/getDocument.aspx?DOCNUM=37029762">http://idbdocs.iadb.org/wsdocs/getDocument.aspx?DOCNUM=37029762</a>   |
| 2.                  | Economic analysis<br><a href="http://idbdocs.iadb.org/wsdocs/getDocument.aspx?DOCNUM=37029077">http://idbdocs.iadb.org/wsdocs/getDocument.aspx?DOCNUM=37029077</a>   |
| 3.                  | Execution arrangements<br><a href="http://idbdocs.iadb.org/wsdocs/getDocument.aspx?DOCNUM=37069894">http://idbdocs.iadb.org/wsdocs/getDocument.aspx?DOCNUM=37069894</a>  |
| 4.                  | Itemized program costs<br><a href="http://idbdocs.iadb.org/wsdocs/getDocument.aspx?DOCNUM=37028924">http://idbdocs.iadb.org/wsdocs/getDocument.aspx?DOCNUM=37028924</a>  |
| 5.                  | Unanimous favorable opinion from the Special Standing Committee on Science, Technology, and Education<br><a href="http://idbdocs.iadb.org/wsdocs/getDocument.aspx?DOCNUM=37119376">http://idbdocs.iadb.org/wsdocs/getDocument.aspx?DOCNUM=37119376</a> |
| 6.                  | Safeguards Policy Filter and Screening Form<br><a href="http://idbdocs.iadb.org/wsdocs/getDocument.aspx?DOCNUM=37130985">http://idbdocs.iadb.org/wsdocs/getDocument.aspx?DOCNUM=37130985</a>   |
| <b>BIBLIOGRAPHY</b> |  |
| 1.                  | Bibliographical sources<br><a href="http://idbdocs.iadb.org/wsdocs/getDocument.aspx?DOCNUM=37104433">http://idbdocs.iadb.org/wsdocs/getDocument.aspx?DOCNUM=37104433</a>   |

## **ABBREVIATIONS**

|        |  |
|--------|--|
| ESMP   | Environmental and social management plan   |
| FONABE | Fondo Nacional de Becas [National Scholarship Fund]  |
| MEP    | Ministry of Public Education   |
| OECD   | Organisation for Economic Co-operation and Development   |
| PISA   | Programme for International Student Assessment   |
| PMR    | Progress monitoring report   |
| PSU    | Project Supervision Unit   |
| SDI    | Social development index   |
| SERCE  | Segundo Estudio Regional Comparativo y Explicativo [Second Regional Comparative and Explanatory Study] |
| SUGEF  | Superintendencia General de Entidades Financieras [General Superintendency of Financial Entities]      |
| WAL    | Weighted average life  |

## PROJECT SUMMARY

### COSTA RICA EDUCATION INFRASTRUCTURE CONSTRUCTION AND EQUIPMENT (CR-L1053)

| Financial Terms and Conditions   |                      |   |   |
|--|----------------------|---|---|
| <b>Borrower:</b> Trust to be set up by the Republic of Costa Rica, represented by a public bank to be selected as trustee, or any successor or entity that substitutes for or replaces it as trustee<br><b>Guarantor:</b> Republic of Costa Rica<br><b>Executing agency:</b> Borrower  |                      | <b>Flexible Financing Facility*</b>     |   |
|  |                      | Amortization period:                    | 20 years  |
|  |                      | Original weighted average life:         | 12.75 years   |
|  |                      | Disbursement period:                    | 5 years   |
|  |                      | Grace period:                           | 5.5 years   |
| <b>Source</b>  | <b>Amount (US\$)</b> | Inspection and supervision fee:         | **  |
| IDB (OC)   | 167,000,000          | Interest rate:                          | LIBOR-based   |
| Local  | 0                    | Credit fee:                             | **  |
| Total  | 167,000,000          | Currency:                               | U.S. dollars from the Bank's Ordinary Capital   |
| Project at a Glance  |                      |   |   |
| <b>Project objective:</b> The general objective of the program is to improve the physical conditions of education infrastructure, the learning environments, and the internal efficiency of beneficiary primary and secondary schools by providing infrastructure to schools that currently lack their own (see paragraph 1.21).<br><b>Special contractual conditions precedent to the first disbursement of the financing:</b> (i) the signing and entry into force of the lease contract under the terms agreed upon with the Bank; (ii) designation of the monitoring unit by the Ministry of Public Education; and (iii) adoption of the Operations Manual specifying the roles, processes, and responsibilities of entities involved in the operation, and including measures to manage and control environmental and social impacts as described in the Environmental and Social Management Report (see paragraph 3.6).<br><b>Special contractual conditions for execution:</b> (i) the bond issue and any public or private borrowing by the borrower requires the Bank's written consent (see paragraph 3.3); (ii) the lease contract will provide for the obligation that the lessee make a termination payment to the trust in an amount sufficient to cover the amount owed to the Bank; and (iii) termination of the lease contract or of the trust and the substitution, replacement, or change of the trustee without prior written consent from the Bank will empower the Bank to suspend loan disbursements, accelerate repayment of the balance on the loan, and cancel the undisbursed portions of the loan (see paragraph 2.4). |                      |   |   |
| <b>Exceptions to Bank policies:</b> None   |                      |   |   |
| <b>Project qualifies as:</b>   |                      | SEQ <input checked="" type="checkbox"/> | PTI <input type="checkbox"/> Sector <input type="checkbox"/> Geographic <input type="checkbox"/> Headcount <input type="checkbox"/> |

\* Under the Flexible Financing Facility (FN-655-1), the borrower has the option of requesting changes to the amortization schedule, as well as currency and interest rate conversions. In considering such requests, the Bank will take operational and risk-management considerations into account.

\*\* 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.

## I. DESCRIPTION AND RESULTS MONITORING

### A. Background, problems to be addressed, and rationale

- 1.1 **Primary challenges in the sector.** Costa Rica has made significant progress in both the quality and coverage of education: 100% of children attend primary school, 95% of the population is literate, and regional standardized tests in reading and mathematics place the country among the region's leaders. For example, Costa Rica was one of the highest-scoring countries in both math and reading on the Second Regional Comparative and Explanatory Study (SERCE). Also scoring highly on the SERCE were Cuba, Chile, Mexico, and Uruguay. Despite this progress, however, the education system still faces major challenges related to quality of learning, internal efficiency, and equity, especially at the secondary level.
- 1.2 **Quality of learning.** In Latin America, Costa Rica is one of the highest-scoring countries on international tests. This is not the case, however, when the country is compared with developed and developing countries in other regions. On the 2009 standardized test of the Programme for International Student Assessment (PISA),<sup>1</sup> 67% of Costa Rican 15-year-olds achieved the minimum competencies in reading necessary to be able to participate effectively and productively in society, compared with an average of 52% among Latin American countries and 81% among countries of the Organisation for Economic Co-operation and Development (OECD). In math, only 43% of Costa Rican students achieved minimum competencies. Among Latin American countries, only Chile scored higher than Costa Rica; other participating countries had a lower percentage of students achieving these competencies. However, Costa Rica ranked 44th in reading and 55th in math out of all 75 countries participating in the PISA (OECD 2012, bibliographic [electronic link #1](#)).<sup>2</sup>
- 1.3 **Efficiency, equity, and coverage.** The internal efficiency of the education system is another major challenge facing the sector. Costa Rica's school failure rate, as measured by the percentage of students who flunk or drop out, is high compared with other countries in the region. While 13.7% of first-graders flunked, this rate rises sharply at the secondary level, where 27.1% of all seventh-graders (secondary school) and 21.8% of all secondary school students flunked in 2010. Of those who flunk, some drop out while the rest repeat the grade, causing major inefficiencies in the education system. Though the dropout rate is low at the primary level (2.8%), one out of every 10 secondary school students (10.2%) and 16.5% of all seventh-graders drop out. There are also challenges involving equity, related to where students live and what their socioeconomic level is.
- 1.4 School failure at the primary level means that a significant percentage of students enter secondary school at a higher-than-expected age. For example, 18.1% of all seventh-graders are 15 or older, when the expected age at that grade is 13. On

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<sup>1</sup> Ten countries participated in the 2010 PISA test (PISA 2009+), and these scores were compared to those of the 65 participating countries that took the same test in 2009.

<sup>2</sup> All bibliographic sources cited in this document can be found in bibliographic electronic link #1.

average, one in every five secondary school students is at least two years older than expected. This places them in a special risk situation, as the pressure on them to enter the labor market increases as they grow older. There are also notable discrepancies between areas with a different social development index (SDI);<sup>3</sup> for example, 16.9% of first-graders in schools located in areas with a very low SDI flunk, compared with 10.6% of students from schools in high-SDI districts. A similar pattern holds true for dropouts.

- 1.5 Internal inefficiency (student failure and dropout) causes a high incidence of delayed and overage students, which eventually leads to low secondary-school graduation rates. Costa Rica has one of the lowest rates of secondary-school completion rates in the region: only 45% of people ages 20 to 24 have completed secondary school (12 years of education). Average educational attainment in 2010 for people above age 15 was 8.4 years nationwide; in rural areas it was only 7.0 years, compared with 9.3 years in urban areas (State of the Nation Program, 2011, bibliographic [electronic link #1](#)). This is in part because secondary schools are less available and of lower quality in rural areas than in urban areas.
- 1.6 The Ministry of Public Education (MEP) has identified the leading causes of inefficiency and poor quality, including an outdated curriculum, deficient in-service teacher training, weaknesses in how the education system and individual schools are managed, and a lack of education infrastructure, as well as student-based problems, such as a lack of cultural capital and financial resources. Moreover, secondary education is of limited availability in rural and periurban areas.
- 1.7 **Government policies to improve quality and equity in the education system.** The MEP has undertaken a number of reforms in recent years to address the aforementioned challenges. To improve quality, it began reforming math and language arts curricula by introducing changes from the preschool level through the end of secondary school. These reforms have been accompanied by a strong in-service teacher training program, changes in how courses are evaluated, and diagnostic assessments to identify areas for improvement, among others. Along these lines, the MEP has launched such programs as “*El Cole en tus Manos*” [Secondary School in Your Hands], “*Escuelas Prioritarias*” [Priority Primary Schools], and “*Ética, Estética y Ciudadanía*” [Ethics, Aesthetics, and Citizenship] to provide further support to academically at-risk children and young people. These programs also seek to forge stronger ties between students and their schools, empowering them to mitigate their risk of dropping out. The MEP also carried out one of the sector’s most significant reforms in recent decades by amending the rules governing evaluations at the secondary school level (Decree 34886-MEP). This provided flexibility in grade-level promotion at the secondary level by allowing students to retake only those courses they had failed in the preceding school year. Before this reform, a student who failed 1 out of 14 classes had to repeat the entire

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<sup>3</sup> The SDI consists of four dimensions: education, health, social participation, and economics. The index ranges from 0 to 100.

year, which led to higher dropout rates (Wendy Jiménez and Marcelo Gaete, 2010, bibliographic [electronic link #1](#)).

- 1.8 To eliminate the economic barriers to education access for students of low socioeconomic status, the government has strengthened and promoted programs such as the National Scholarship Fund and the *Avancemos* Program, which provide financial support to more than 360,000 students (25.4% of all public school students). The government also provides a subsidy to feed children in school cafeterias; the poorest families are subsidized at 100%.<sup>4</sup> These policies have succeeded in reducing school failure and improving access for the lower-income population. The percentage of children age 13 to 17 enrolled in school rose from 71% to 80% among the poorest quintile in terms of income, from 74% to 83% for the second-poorest quintile, and from 80% to 87% for the middle quintile. Moreover, the dropout rate among secondary school students fell from 14.3% in 2000 to 13.8% in 2010.
- 1.9 The MEP has also made significant changes in education system management, from the school level to the central level. In 2006 it began the process of restructuring the central level of the MEP and in 2012 started a program titled “*Más Educación y Menos Papeleo*” [More Education, Less Paperwork], which will identify the processes, functions, and responsibilities of the various levels of the education system to simplify them and even eliminate any redundant ones. This will lessen the administrative burden on teachers, administrators, and other officials, allowing time and resources to be spent on improving the quality of education.
- 1.10 **Education infrastructure, the task at hand.** In the process of improving quality and equity in education, one of the MEP’s biggest challenges has been the education infrastructure deficit. Higher retention and promotion rates have increased the need for infrastructure, and programs such as those described above have been hindered by a lack of facilities to accommodate students’ athletic, recreational, artistic, and extracurricular activities. These deficiencies are in addition to the country’s “historical deficit” in school infrastructure, which is deemed “one of the critical problems in the Costa Rican education system today” (State of the Nation Program, 2011, bibliographic [electronic link #1](#)). This deficit equates to some US\$1 billion, including 7,658 classrooms, 7,437 restrooms, 1,130 libraries and resource centers, 924 cafeterias, 1,072 computer labs, and 1,001 teachers’ lounges, among others. Moreover, some 2,127 classrooms (6.8% of all existing classrooms) have been identified as being in “poor condition.”
- 1.11 The MEP has made considerable efforts to overcome this deficit. Budgeting for these efforts rose nearly 400% between 2006 and 2010 (from US\$11.2 million to US\$56.6 million, approximately). School construction increased from 48,324 square meters in 2007 to 115,971 square meters in 2010, an increase of

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<sup>4</sup> Regular students are charged about US\$0.40 per day for food. The poorest students receive a 100% subsidy and do not pay for food.



- about 140%.<sup>5</sup> The budget for furniture purchases rose from US\$1.2 million in 2006 to US\$3.8 million in 2010, an increase of more than 200%. This progress, however, has not been enough to bridge the education infrastructure gap.
- 1.12 For example, 29.6% of primary school classrooms in urban areas, and 40.4% in rural areas, are in fair/poor condition. In nine cantons, a majority of the classrooms are in fair/poor condition. Two of these are in the province of Alajuela (San Mateo, 71.4%; Orotina, 63.3%), four are in Guanacaste (Nicoya, 63.4%; Abangares, 60.4%; Hojancha, 59.9%; and Nandayure, 54.8%); two are in San José (Goicochea, 53.1%; Puriscal, 52.3%); and one is in Limón (Talamanca, 52.1%). There are 1,434 public primary schools nationwide where more than 50% of the classrooms are in fair/poor condition. This represents two out of every five public primary schools.
- 1.13 Costa Rican students cite deficiencies in physical infrastructure as one of the main causes of hostile situations at school, which in some cases even lead to violence (León, A.T., 2010, bibliographic [electronic link #1](#)). The poor condition of facilities is identified by 40.9% of secondary school students as their school's biggest problem, with 28.7% citing the poor condition of restrooms. In fact, 8 of the 12 most common spontaneous responses as to the schools' biggest problems are related to infrastructure (UNIMER, 2009, bibliographic [electronic link #1](#)). This is also reflected in the opinions of teachers, 70% of whom are dissatisfied with the condition of the infrastructure, and 75% cite the poor condition of the restrooms. In addition to the aforementioned problems related to curriculum and quality of teaching, the poor condition of physical infrastructure for education could be creating an unhealthy school environment and hindering the learning process. Indeed, 15- to 17-year-old secondary school students report various types of problems in their relationship with their school, including not only academic difficulties (26%) but also problems with teachers (26%) and peers (17%).
- 1.14 The international literature on education infrastructure and quality indicates that school facilities have an impact on teacher motivation and on student behavior and learning (Schneider, M., 2002 bibliographic [electronic link #1](#)). Regional studies have found that the physical conditions of schools have a significant impact on student performance and learning (Duarte, J., Gargiulo, C., and Moreno, M., 2011, bibliographic [electronic link #1](#)). Infrastructure problems not only hinder academic performance, they also create a hostile environment that can have a harmful effect on interpersonal relationships and can even lead to violence. They can have negative repercussions on students' self-esteem and sense of dignity, especially when the sanitary infrastructure is not appropriate (State of the Nation Program, 2011, bibliographic [electronic link #1](#)). Other research has found that overcrowding and a lack of recreational facilities increase stratification and inequity and generate conflicts in the school community (Ready, D., Lee, V., and Welner, K. G., 2004,

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<sup>5</sup> Starting in 2006, more resources were allocated to building entire schools, as opposed to adding classrooms to existing schools. As such, no direct correlation exists between investment and reduction of the infrastructure deficit. Furthermore, the cumulative inflation rate for 2006-2010 was 52%.

bibliographic [electronic link #1](#)). These factors indirectly contribute to students' decisions to drop out of school (Jiménez, W., and Gaete, M., 2010 bibliographic [electronic link #1](#)).

- 1.15 The reforms promoted by the MEP have been limited by the buildings' deficiencies. It has not been possible to implement programs such as "Ethics, Aesthetics, and Citizenship" in all prioritized establishments due to lack of space. Moreover, flexible promotion has increased the need for education facilities, the absence of which has limited the supply of academic and recreational activities for students who are not taking a full course load. In turn, the return of students as a result of the reforms has produced greater overcrowding in some schools. As a result, the infrastructure deficit: (i) is discouraging to students; (ii) prevents the introduction of curricular improvements; and (iii) makes it impossible to offer special academic programs and additional classes for students who are only repeating certain courses. All of this leads to student dropout.
- 1.16 **The Bank's other loan operations in the sector.** The Bank has six technical-cooperation operations supporting the sector. The most recent loan, approved in September 1998, was the "Preschool and Lower Secondary Education" program (CR-0044) (loan 1010/OC-CR) for US\$28 million, which concluded satisfactorily in December 2005. This new operation will continue that program's efforts. In part the delay in execution was caused by weaknesses in the executing unit, which was immersed in the MEP's complex institutional dynamics. This has also caused delays in other operations, such as the World Bank's Equity and Efficiency in Education project, which dates from 2005 and is only 56% disbursed. This operation will coordinate with other cooperation agencies, particularly the World Bank, UNICEF, and the European Union, in order to share experiences and lessons learned.
- 1.17 **Program strategy.** This operation will help reduce the country's education infrastructure deficit by enhancing and expanding learning environments and improving the internal efficiency of beneficiary schools, through the provision of infrastructure to schools that currently lack their own and the construction of new schools in densely populated areas. The program will address approximately 20% of the current deficit.
- 1.18 To this end, the Executive Branch will establish a public works trust at one of Costa Rica's four State-owned banks.<sup>6</sup> The trust is an innovative mechanism that will make it possible to streamline the construction and maintenance of the schools to be built by the program. It is the first operation of this nature on the part of a

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<sup>6</sup> These banks are Banco Nacional de Costa Rica, Banco de Crédito Agrícola de Cartago, Banco Popular, and Banco de Costa Rica. The trustee bank will be selected after the law is enacted. All four banks have been confirmed to be in compliance with the Bank's Eligible Borrowers Policy (OP-301).

central government entity,<sup>7</sup> after a series of positive experiences by state entities like the Costa Rican Electricity Institute. The trust will be responsible for building 79 complete schools (69 for currently operating schools and 10 for new schools) and cultural and athletic facilities to promote recreation and sports at 24 currently operating schools. The 69 primary and secondary schools already in operation were selected on the basis of two basic criteria: (i) schools lacking their own infrastructure (they rent or lease the space they use); and (ii) schools whose own facilities are irreparable or are located in high-risk areas as determined by the National Emergency Commission. The 10 new schools will be built in densely populated districts with unmet demand at the secondary school level. The 24 schools where cultural and athletic facilities will be built were given priority on the basis of the density of their student population and the lack of nearby recreational and athletic facilities. Eighty-three percent of the districts in which new schools will be built have an SDI below 60%, and the schools to be served by the program have a lower internal efficiency than other public schools, even lower than those in low-SDI districts.

- 1.19 The replacement of subpar schools and classrooms and the construction of recreational and athletic facilities are expected to yield an improved school environment and more motivated teachers and students. This will help reduce conflicts in school, improve teachers' classroom management, enhance student performance, and, as a result, increase the internal efficiency of the education system as evidenced in lower student failure and dropout rates. This, in turn, is expected lead to better student learning. The aforementioned studies support these expectations, as they link improvements in physical infrastructure to greater student and teacher motivation, fewer conflicts, and improved performance.
- 1.20 **Alignment with the country strategy and GCI-9.** Education is one of the priority areas of dialogue with the country identified in the 2011-2014 Country Strategy with Costa Rica (document GN-2627; paragraph 3.2). This operation stems from the deepening of that dialogue. The program is aligned with the Ninth General Increase in the Resources of the Inter-American Development Bank (document AB-2764) and the Sector Guidelines for Education (document GN-2614). At the same time, it contributes to deepening the dialogue for future interventions in the country. Some 35,000 students who live in low SDI areas will benefit directly. The program is part of the 2011-2014 National Development Plan, specifically the social welfare component.

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<sup>7</sup> The trust will make it possible to distribute the risks associated with executing works; the government retains the risks inherent in its regulatory and supervisory functions and transfers the other risks to the trust and the construction firms. In view of the complexity of public administration, particularly of a ministry of education, the program allows for total concentration and a high degree of specialization by staff in the procurement processes. The following observations were made in earlier MEP projects, such as CR-0044 (loan 1010/OC-CR): (i) less than full attention to the project by the line staff; (ii) a lack of experience in applying the procurement rules of the financing entity; and (iii) parallel implementation of the country's and the financing entity's rules. All this has resulted in execution delays.

## **B. Objectives, components, and cost**

- 1.21 The general objective of the program is to improve the physical conditions of education infrastructure, the learning environments, and the internal efficiency of beneficiary primary and secondary schools by providing infrastructure to schools that currently lack it.<sup>8</sup> To this end, direct financing will be provided to build and equip school infrastructure through a public works development trust.
- 1.22 The specific objectives are: (i) to promote the gradual consolidation of a high-quality physical and technological platform to support the transformation of the teaching/learning process; (ii) to reduce the education infrastructure deficit; and (iii) to implement an alternative financing mechanism to address the demand for education infrastructure in a more flexible and timely manner, through long-term financing instruments.
- 1.23 **Component 1. Construction and equipping of primary schools, special education schools, and general basic education institutes in periurban and rural areas.** This component will finance the construction of new buildings for 17 primary, special education, and basic education schools that are currently operating in rented or borrowed infrastructure (multipurpose halls, churches, etc.) and that are in poor condition. It will be executed in three phases: in the first, coinciding with the second year of program execution, six schools will be built; in the second, six schools; and in the third, five schools.
- 1.24 Of the 17 schools to be built, two serve 1,000 special education students in the cantons of Santa Ana (San José) and Guácimo (Limón). Thirteen schools serve some 5,000 primary school students (first to sixth grades) in 13 cantons in the provinces of San José, Heredia, Cartago, Limón, Guanacaste, and Puntarenas. Two general basic education institutes (first to ninth grades), serving some 1,550 students, will be built in Desamparados (San José) and Nandayure (Guanacaste).
- 1.25 The schools to be built will include classrooms, restrooms, administrative areas, a cafeteria, recreational facilities and complementary works and, depending on enrollment, a school library and computer lab. Current enrollment at these schools is 7,526; once improved and expanded, they will be able to accommodate some 8,450 students. The schools' capacities range from 150 to 1,900 students, with an average capacity of 497 students per school. Financing will also be provided for the purchase of five plots of land for building the schools. The other 12 schools have MEP-owned land, and the right to use this land will be transferred to the trust. Financing will also be provided for furniture and equipment based on current national standards and regulations.

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<sup>8</sup> Primary schools in Costa Rica are called *escuelas*, and secondary schools are termed *colegios*. Schools providing vocational education are known as *colegios técnicos profesionales*. Secondary schools in rural areas are called *liceos rurales* [rural secondary schools] or *telesecundarias* [distance-learning secondary schools]. Combined primary and lower secondary schools are known as *unidades pedagógicas* [pedagogical units] or *institutos generales de educación básica* [general basic education institutes].

- 1.26 **Component 2. Construction and equipment of secondary schools in rural and periurban areas.** This component will finance construction of new buildings for 52 academic secondary schools, rural secondary schools and distance-learning secondary schools, and vocational education schools that are currently operating in rented or borrowed infrastructure (multipurpose halls, churches, etc.) and that are in poor condition. It will also finance construction of 10 new buildings to house new schools in densely populated areas where existing schools are overcrowded. As with Component 1, this component will be executed in three phases: in first phase, coinciding with the second year of the program, 16 schools will be completed; in the second, 19 schools; and in the third, 27 schools.
- 1.27 Of the 52 schools to be built, 35 (67%) will be rural secondary schools or distance-learning schools, with a total enrollment of 2,408 students and an average of 69 students per school. The other 17 schools are regular secondary schools (grades 7 to 11) in periurban and rural areas, which serve 3,878 students and have an average enrollment of about 228 students per school. The 10 new schools to be built will be located in densely populated periurban areas: five will be regular secondary schools (grades 7 to 11), and the other five will be vocational schools (grades 10 to 12). These schools will have an average capacity of 850 students.
- 1.28 The schools to be built will include classrooms, restrooms, administrative areas, a cafeteria, and recreational facilities. They will also include complementary works such as gardens, security booths and fencing, a school library and computer and science lab, depending on the size of the school. Financing will also be provided for the purchase of 38 plots of land and the provision of furniture and equipment, whose quality and specifications will be consistent with current national regulations and standards issued by the MEP. The program will also finance the hiring of individual consultants and consulting firms to develop, evaluate, and supervise the construction work.
- 1.29 **Component 3. Construction of cultural and athletic facilities in schools with large student populations.** This component will finance the provision of cultural and athletic facilities to promote sports, art, culture, and recreation through strategic investments in infrastructure to make schools more appealing to students and teachers, instill them with a greater sense of rootedness and belonging, and allow for the development of skills and abilities to help reduce school failure. This component will finance the provision of facilities at 24 schools: one primary school, 10 regular secondary schools in periurban areas, and 13 vocational schools in urban, periurban, and rural areas.
- 1.30 The 24 cultural and athletic facilities will benefit more than 13,200 students. The schools where they will be built have large student populations, with an average of 550 students per school. This component will be executed in two phases: most of the facilities (18 out of 24) will be completed in the first phase, coinciding with the second year of program execution. For these schools, the plots of land will be separated from the larger properties and the right to use them will be granted to the trust, which will be responsible for the construction work.

- 1.31 The design, construction, and equipment of the schools and acquisition of the plots of land for the project will follow the guidelines established by the MEP, provided they are consistent with the provisions of the loan contract and with applicable Bank policies.
- 1.32 **Administration, supervision, and other operating costs.** The program will finance the executing unit or the cost of a procurement agency, either of which, as applicable, will be responsible for project procurement. Financing will also be provided for the operation's administrative costs, understood as oversight committee per diem, insurance, and maintenance; permit and licensing procedures; and works supervision. Lastly, this component will cover the costs of external auditing of the trust and, subject to the approval of the Legislative Assembly, may cover the interest payments on the loan during construction.
- C. Key indicators in the results matrix**
- 1.33 The key outcomes expected from this operation include: (i) improved student learning and progress in the beneficiary schools; (ii) an improved school environment in beneficiary schools; (iii) improved promotion rates in beneficiary schools; (iv) reduced dropout rates in beneficiary schools; and (v) increased capacity in secondary schools in the areas where the new secondary schools will be built. The program's output and outcome indicators are detailed in Annex II.
- 1.34 **Costs and financing.** The cost of the program is US\$167 million, with an execution period of four years. Table I-1 summarizes program costs; for more details, see optional [electronic link #4](#).

**Table I-1: Program costs (in US\$)**

| Category of spending per component                             | IDB                | TOTAL              | %            |
|--|--------------------|--------------------|--------------|
| 1. Construction and equipment of primary schools               | 30,883,195         | 30,883,195         | 18.5         |
| 2. Construction and equipment of secondary schools             | 116,274,206        | 116,274,206        | 69.6         |
| 3. Construction of cultural and athletic facilities            | 8,870,016          | 8,870,016          | 5.3          |
| Financial costs, administration, monitoring, and contingencies | 10,972,583         | 10,972,583         | 6.6          |
| <b>TOTAL</b>   | <b>167,000,000</b> | <b>167,000,000</b> | <b>100.0</b> |

## **II. FINANCING STRUCTURE AND RISKS**

### **A. Financing instruments**

- 2.1 The project will be financed by an investment loan to the selected State-owned bank, in its capacity as trustee of a public works development trust to be established by the Government of Costa Rica. Loan disbursements will begin in 2013. In its capacity as trustor, the Government of Costa Rica will make an in-kind contribution in the form of school infrastructure drawings and models, as well as the right to use the plots of land provided to the trust. In addition, the Government of Costa Rica and the selected State-owned bank, in its capacity as trustee, will sign a lease

contract for the use of these works; payment of this lease by the Government of Costa Rica will provide the cash flow that will allow the trust to repay the Bank's loan. The costs associated with performance of the trustee's role, along with insurance and bonds, *inter alia*, will be covered directly by the Government of Costa Rica, and may not exceed 2% of the total project cost per year, as set forth in the proposed legislation (see paragraphs 3.1 and 3.2).

**Table II-1: Disbursement timetable (in US\$ million)**

| Source       | Year 1              | Year 2              | Year 3              | Year 4              | Total                |
|--------------|---------------------|---------------------|---------------------|---------------------|----------------------|
| IDB          | 16.48               | 63.32               | 65.90               | 21.30               | 167.00               |
| <b>Total</b> | <b><u>16.48</u></b> | <b><u>63.32</u></b> | <b><u>65.90</u></b> | <b><u>21.30</u></b> | <b><u>167.00</u></b> |

## **B. Risks**

- 2.2 **Environmental and social risks.** In accordance with the Environment and Safeguards Compliance Policy (OP-703), this operation is classified as Category "B," since its potential negative social and environmental impacts are localized and short-term in nature, and mitigation measures are known and easy to implement. Consultation processes will be conducted with the beneficiary communities. The operation will generate positive social impacts, as reflected in higher promotion rates and lower dropout rates, and improvements in the organizational climate in schools and in learning. To mitigate the potential environmental and social impacts, the Operations Manual will include environmental management and control measures. In addition, an Environmental and Social Management Plan will be prepared for each project; and standard practices or regulations will be observed in waste disposal and the recycling of stone materials, as will regulations for reducing risks associated with natural disasters, among others (see Environmental and Social Management Report, required [electronic link #4](#)).
- 2.3 **Fiduciary risks.** Based on the execution arrangements, and given the existing levels of control in the country, this operation is deemed to have a medium level of fiduciary risk (see Annex III). No additional risks have been identified in procurement, especially if a specialized procurement agency is hired for this purpose. Risks related to the nature of the execution arrangements have been identified, in view of the multiple processes and actors involved. Efforts are under way to approve a technical-cooperation operation to help strengthen the MEP for its role in this program.
- 2.4 **Other risks.** Some risks are inherent to the construction of education infrastructure. To cover variations in base construction prices, 5% will be earmarked annually and 8% to cover additional costs of works in rural areas or on broken ground. There is also a risk that the Legislative Assembly will not pass the proposed legislation, which is considered a low risk since the Science, Technology, and Education Committee issued a unanimous "positive report" (optional [electronic link #5](#)). The proposed law therefore moves on to the plenary for discussion and approval. In this regard, the project is much further along in its approval process than a conventional

lending operation. Lastly, there is a risk that a decision is made to cancel the trust or the lease during the life of the loan. The following special contractual conditions for execution are provided to address this risk: (i) the lease contract must include a trust termination payment by the Republic of Costa Rica in an amount sufficient to cover the amount owed to the Bank; and (ii) termination of the lease contract or of the trust will empower the Bank to suspend disbursements of the loan, accelerate repayment of the outstanding balance on the loan, and cancel the undisbursed portions of the loan. The probability that these risks will materialize is low, given the Executive Branch's commitment and the support observed in the Assembly thus far.

### **III. IMPLEMENTATION AND ACTION PLAN**

#### **A. Summary of execution arrangements**

- 3.1 The program will use a novel mechanism for financing and execution. The Government of Costa Rica will establish a trust with financial leasing and will guarantee the Bank's loan in accordance with the proposed legislation entitled "Authorization for the Executive Branch to establish a trust and sign a public finance transaction through a long-term lease agreement to finance the MEP's education infrastructure construction and equipment project throughout the country" (18258) (see execution arrangements, [optional link #3](#)).
- 3.2 This bill was introduced in the Legislative Assembly on 23 September 2011 and is currently being debated in the Science, Technology, and Education Committee. It authorizes the Executive Branch to: (i) sign the public debt contract; (ii) establish a trust to sign the public debt contract and execute construction of the public works; (iii) sign a lease contract for the use of these works (owned by the trust over its lifetime) and for the corresponding lease payment, which will provide the cash flow to enable the trust to service the loan; and (iv) guarantee the obligations assumed by the trust.
- 3.3 The trust contract will be signed by the Government of Costa Rica with one of the four State-owned banks in Costa Rica,<sup>9</sup> which will serve as trustee. The Office of the Comptroller General will endorse the contract. The Bank will sign the loan contract with the trust represented by the trustee bank, and at the same time the Government of Costa Rica will sign a guarantee contract with the Bank to back the obligations of the trust. Changing the trustee institution, in the form of succession, substitution, or replacement, will require the prior written consent of the Bank. The Government of Costa Rica will grant the trust the right to use the land it owns for project-related construction work, in the form of a trust asset. It will also furnish all of the standard drawings, models, and topographical studies it has for these plots of land, which will be part of the initial trust assets. The trust assets will also include:

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<sup>9</sup> The trustee bank will be selected through a shortened procedure (two months) whereby banks will submit expressions of interest and proposals.



- (i) the funds from the loan operation with the Bank; (ii) the built infrastructure; (iii) the procured equipment; and (iv) revenues from the leasing of schools. The proposed legislation authorizes a maximum debt of US\$167.5 million, which means that the program will cover almost the entire project, and no bonds are expected to be issued in the short term. As a special contractual condition for execution, any bond issue must be approved by the Bank.
- 3.4 The State-owned bank that acts as executing agency will establish an executing unit, which will conduct the contracting processes either with its own personnel or through a procurement agent. In such case, this procurement agent will be hired within the framework of the Policies for the Selection and Contracting of Consultants Financed by the Inter-American Development Bank (document GN-2350-9). In any event, the provisions of the loan contract and Bank policies will be followed. The executing unit will provide maintenance for the works over the life of the trust. Meanwhile, the MEP will establish a technical counterpart—the Project Supervision Unit—to monitor execution of the works for which the trust is responsible, and to serve as the primary operational liaison for the MEP. Both the MEP and the Bank will serve as trustees of the trust, with the powers set forth in the Commercial Code and in the signed loan contract. An oversight committee will be formed as the highest authority of the trust, to ensure that the provisions of the trust contract are fulfilled. The Oversight Committee will have representatives from the MEP and the Ministry of Finance at a minimum.
- 3.5 Once the trust is legally established, the Government of Costa Rica and the selected State-owned bank, in its capacity as trustee, will also sign contracts for the leasing of school infrastructure for a 20-year period. The loan will be repaid with revenues from the lease payments to the trust, which will be made directly by the Ministry of Finance from the line items for repayment of public debt. Over the life of the trust, the trustee will provide preventive and major corrective maintenance for the infrastructure that is built. Minor repairs and basic maintenance will be the responsibility of the boards of education and administrative bodies, pursuant to applicable regulations (31024-MEP).
- 3.6 The following will be conditions precedent to the disbursement of the loan: **(i) the signing and entry into force of the lease contract under the terms agreed upon with the Bank; (ii) designation of the monitoring unit by the MEP; and (iii) adoption of the Operations Manual, specifying the roles, processes, and responsibilities of entities involved in the operation, and including measures to manage and control environmental and social impacts as described in the Environmental and Social Management Report.**
- 3.7 **Reporting.** The trust will submit semiannual progress reports to the Bank, which will include, as an annex, the table from the Progress Monitoring Report (PMR). In December of every calendar year during program execution, the trust will submit an annual work plan and an annual procurement plan to the Bank for approval. The contract establishing the trust will set out the reports to be submitted to the Oversight Committee.

- 3.8 **Execution supervision system.** The program will adopt the Bank's supervision and monitoring mechanisms. The project supervision plan will be developed and validated with the borrower, and will include multiyear programming of activities and finances. The MEP will set up a project monitoring unit.

**B. Procurement**

- 3.9 The procurement of goods and works and the selection and hiring of consulting services will be carried out in accordance with Bank policies (documents GN-2349-9 and GN-2350-9), the details of which are set out in the annual procurement plans. For national competitive bidding and shopping processes, documents consistent with the Bank's procurement policies will be agreed upon for goods and works.

**C. Retroactive financing and auditing**

- 3.10 No provision is made for retroactive financing. External auditing will be performed by independent auditors in accordance with terms of reference previously agreed upon with the Bank, financed with resources from the program, and will be commissioned in accordance with document AF-200. The audited annual financial statements must be submitted within 120 days after the end of each fiscal year throughout the life of the program, and the final financial statements must be submitted within 120 days after the last disbursement. The program will finance the audits during the disbursement period, and own resources will be used thereafter.

**D. Monitoring and evaluation**

- 3.11 **Economic evaluation.** The evaluation of the program's cost-effectiveness ([optional link #2](#)) shows that the internal efficiency of beneficiary schools can be substantially improved. Schools are currently performing at a very low level in terms of student progress through primary and secondary school. Completion rates are 53% in primary school (sixth grade) and 36% in secondary school (11th grade). These rates are similar to or below those in public schools located in the cantons with the lowest educational achievement. An improved completion rate resulting from program investments should help reduce the unit cost of completing school in beneficiary primary schools to 72% of current costs. The unit cost of completion at beneficiary secondary schools should be brought down to 64% of current costs. The cultural and athletic facilities are also cost-effective. In primary school, the investment will help reduce the cost of completion per age-appropriate student to 75% of current costs, and in secondary school, to 76%.
- 3.12 **Monitoring, follow-up, and evaluation.** The trust will be responsible for regularly monitoring the fulfillment of the project's work plans, outputs, and outcomes. Monitoring will be based on: (i) the annual work plan; and (ii) the results matrix. The trust will submit semiannual progress reports to the Bank on outputs, as well as annual reports on outcomes, which will include as an annex the table from the PMR. During program execution, a number of qualitative and quantitative evaluations will be conducted to measure achievements in terms of the program's

general objectives. Performance of these evaluations will be subject to the availability of technical cooperation resources and their results will be available upon program completion. The evaluation will seek to determine whether the program has succeeded in improving the learning environments and the internal efficiency of beneficiary establishments through the new education infrastructure (see Monitoring and Evaluation Plan, [optional link #2](#)). Special emphasis will be placed on verifying whether the trust has a positive impact on the execution period.

## Development Effectiveness Matrix Summary

| Development Effectiveness Matrix   |   |  |               |
|--|---|--|---------------|
| Summary  |   |  |               |
| I. Strategic Alignment   |   |  |               |
| 1. IDB Strategic Development Objectives  | Aligned   |  |               |
| Lending Program  | (i) Lending to small and vulnerable countries, and (ii) Lending for poverty reduction and equality enhancement. |  |               |
| Regional Development Goals   | Share of youth ages 15 to19 who complete ninth grade.   |  |               |
| Bank Output Contribution (as defined in Results Framework of IDB-9)  | Students benefited by education projects.   |  |               |
| 2. Country Strategy Development Objectives   | Not Aligned   |  |               |
| Country Strategy Results Matrix  | GN-2627   | The intervention is not aligned with a Country Strategy Objective.   |               |
| Country Program Results Matrix   | GN-2661-4   | The intervention is not included in the 2012 Country Program Document.   |               |
| Relevance of this project to country development challenges (If not aligned to country strategy or country program)  |   | The program responds to a deeper dialogue in the sector in the framework of the Country Strategy with Costa Rica 2011-2014. This operation will support the reduction in the infrastructure deficit existing in the country, improving and increasing school infrastructure, learning environments and the internal efficiency of beneficiary schools. |               |
| II. Development Outcomes - Evaluability  | Highly Evaluable  | Weight   | Maximum Score |
|  | 9.5   |  | 10            |
| 3. Evidence-based Assessment & Solution  | 9.8   | 25%  | 10            |
| 4. Ex ante Economic Analysis   | 10.0  | 25%  | 10            |
| 5. Monitoring and Evaluation   | 8.1   | 25%  | 10            |
| 6. Risks & Mitigation Monitoring Matrix  | 10.0  | 25%  | 10            |
| Overall risks rate = magnitude of risks*likelihood   | Medium  |  |               |
| Environmental & social risk classification   | B   |  |               |
| III. IDB's Role - Additionality  |   |  |               |
| The project relies on the use of country systems (VPC/PDP criteria)  |   |  |               |
| The project uses another country system different from the ones above for implementing the program   | Yes   | The program will use a new financing and executing mechanism, as a function of the structuring of a trust fund to develop public works with a lease quote to be constructed by the Republic of Costa Rica.   |               |
| The IDB's involvement promotes improvements of the intended beneficiaries and/or public sector entity in the following dimensions:   |   |  |               |
| Gender Equality  |   |  |               |
| Labor  |   |  |               |
| 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             | Yes   | CR-T1092.  |               |
| 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 has the goal of improving school infrastructure, learning environments and the internal efficiency of schools. The goal would be achieved by financing the construction and equipment of schools through a trust of public works. The program aims to attend 17% of the infrastructure deficit. Regarding the diagnose, it justifies the project around the dropout and failure rates (27% and 17% of 7th graders). It has been observed that 30% of classrooms are in a deficient state. This situation is attributed to low historical investment and increase in demand. The evidence on the effects of infrastructure on failure and dropout rates is weak but in a direction consistent with the justification of the project. The results matrix has a congruent vertical logic. The impact indicators are not aligned to the country strategy because the country strategy does not include indicators in the education sector. The results and one of the impact indicators do not have a baseline. Indicators are SMART and have a data source.

The project has an Ex Ante Cost-Effectiveness Analysis. A quasi experimental evaluation is proposed using matching and differences in differences methodology.

Regarding risks, all identified risks are classified as medium and are associated to management, monitoring and development. The trust feature of the implementation will allow to contract specialized services to the executing unit and decrease risks.

## RESULTS MATRIX

| <b>Project objective</b>            | The general objective of the program is to improve the physical conditions of education infrastructure, learning environments, and the internal efficiency of beneficiary primary and secondary schools by providing infrastructure to schools that currently lack it. To this end, direct financing will be provided to build and equip school infrastructure through a public works trust. |  |  |
|-------------------------------------|--|--|--|
| Purposes                            | Baseline   | Final target   | Comments   |
| Dropout rate at beneficiary schools | Beneficiary primary schools <sup>1</sup> : 1.51%<br>Beneficiary secondary schools <sup>2</sup> : 8.29%   | Beneficiary primary schools: 2% improvement<br>Beneficiary secondary schools: 5% improvement | <p>Average for all grades at each level of schooling, weighted by number of students per school.</p> <p><b>Formula:</b></p> $\sum_{i=1}^n \frac{Des_i}{Mat_i} \times \frac{Mat_i}{Mat_b} = \sum_{i=1}^n \frac{Des_i}{Mat_b}$ <p>Where, for primary and secondary schools:</p> <p><b>Des<sub>i</sub></b> = Total dropouts for grades 1-6 at primary schools and grades 7-12 at secondary schools for beneficiary school <i>i</i>.</p> <p><b>Mat<sub>i</sub></b> = Total enrollment for grades 1-6 at primary schools and grades 7-12 at secondary schools for beneficiary school <i>i</i>.</p> <p><b>Mat<sub>b</sub></b> = Total enrollment for grades 1-6 at primary schools and grades 7-12 at secondary schools for all beneficiary schools.</p> <p>n = total number of beneficiary schools</p> <p><b>Source:</b> Statistical data systems of the Ministry of Public Education.</p> <p>This variable will be disaggregated by gender as soon as the final education statistics for 2011 are available.</p> |

<sup>1</sup> The dropout and failure rate covers the six years of primary school of the Sotero González Pedagogical Unit. The two specialized education centers are excluded.

<sup>2</sup> The dropout and failure rates for secondary schools include the three grades of secondary school at the Sotero González Pedagogical Unit.

|                                     |  |  |  |
|-------------------------------------|--|--|--|
| Failure rate at beneficiary schools | Beneficiary primary schools: 14.05%<br>Beneficiary secondary schools: 17.84% | Beneficiary primary schools: 5% improvement<br>Beneficiary secondary schools: 7% improvement | <p>Average for all grades at each level of schooling, weighted by number of students per school.</p> <p><b>Formula:</b></p> $\sum_{i=1}^n \frac{Rep_i}{Mat_i} \times \frac{Mat_i}{Mat_b} = \sum_{i=1}^n \frac{Rep_i}{Mat_b}$ <p>Where:</p> <p><math>Rep_i</math> = Total number of failing students in grades 1-6 at beneficiary primary school <math>i</math>.</p> <p><math>Mat_i</math> = Total enrollment in grades 1-6 at beneficiary primary school <math>i</math>.</p> <p><math>Mat_b</math> = Total enrollment in grades 1-6 in all beneficiary primary schools.</p> <p><b>Source:</b> MEP statistical data systems.</p> <p>This variable will be disaggregated by gender as soon as the final education statistics for 2011 are available.</p> |
|-------------------------------------|--|--|--|

|  | Baseline | Year 1 | Year 2 | Year 3 | Year 4 | Final target | Comments                          |
|--|----------|--------|--------|--------|--------|--------------|-----------------------------------|
| <b>Component 1: Construction and equipping of primary schools, special education schools, and general basic education institutes</b> |          |        |        |        |        |              |                                   |
| <b>Outputs</b>   |          |        |        |        |        |              |                                   |
| Number of primary schools built and equipped   |          |        | 5      | 4      | 4      | 13           | Source: Program status reports.   |
| Number of pedagogical units (complete basic general education, 1st to 9th grades) built and equipped                                 |          |        |        | 1      | 1      | 2            | Source: Program status reports.   |
| Number of special education centers built and equipped   |          |        | 1      | 1      |        | 2            | Source: Program status reports.   |
| Number of additional seats created in existing schools   | 5,848    |        | 817    | 1,349  | 436    | 8,450        | Source: MEP education statistics. |

|   | Baseline                             | Year 1 | Year 2 | Year 3 | Year 4 | Final target                           | Comments   |
|---|--------------------------------------|--------|--------|--------|--------|--|--|
| <b>Outcomes</b>   |                                      |        |        |        |        |  |  |
| Improved school environment index in beneficiary schools  | To be determined at start of program |        |        |        |        | 10% improvement in index over baseline | <p>The school environment index combines several factors, including interpersonal relationships, the creative environment, and quality of learning, and is based on the perceptions of students, teachers, and administrators.</p> $ICE_{c,e} = \sum_{i=1}^n X_i P_i$ <p>Where:<br/> <math>ICE_{c,e}</math> = School climate index for category <math>c</math> and respondent type <math>e</math>.<br/> <math>X_i</math> = Vector of variables comprising the index for each category and respondent type for each school <math>i</math>. The variables will be estimated using surveys designed for students, teachers, and principals.<br/> <math>P_i</math> = Vector of relative weights associated with each variable. Weights will be estimated using the methodology chosen for the evaluation.<br/> Source: Program survey.</p> |
| <b>Component 2: Construction and equipment of secondary schools in rural and periurban areas</b>                      |                                      |        |        |        |        |  |  |
| <b>Outputs</b>  |                                      |        |        |        |        |  |  |
| Number of rural secondary schools ( <i>liceos</i> ) replacing distance-learning secondary schools, built and equipped |                                      |        | 9      | 13     | 13     | 35                                     | Source: Program status reports.  |
| Number of vocational schools built and equipped   |                                      |        | 1      |        | 4      | 5                                      | Source: Program status reports.  |
| Number of secondary schools built and equipped  |                                      |        | 6      | 6      | 10     | 22                                     | Source: Program status reports.  |
| Number of additional seats created in existing secondary schools and new schools                                      | 3,607                                |        | 980    | 1,545  | 1,578  | 7,710                                  | Source: Program status reports.  |

|  | Baseline                             | Year 1 | Year 2 | Year 3 | Year 4 | Final target   | Comments   |
|--|--------------------------------------|--------|--------|--------|--------|--|--|
| <b>Outcomes</b>  |                                      |        |        |        |        |  |  |
| Improved school environment index in beneficiary schools                                       | To be determined at start of program |        |        |        |        | 10% improvement in index over baseline                   | <p>The school environment index combines several factors, including interpersonal relationships, the creative environment, and quality of learning, and is based on the perceptions of students, teachers, and administrators.</p> $ICE_{c,e} = \sum_{i=1}^n X_i P_i$ <p>Where:<br/> <math>ICE_{c,e}</math> = School climate index for category <math>c</math> and respondent type <math>e</math>.<br/> <math>X_i</math> = Vector of variables comprising the index for each category and respondent type for each school <math>i</math>. The variables will be estimated using surveys designed for students, teachers, and principals.<br/> <math>P_i</math> = Vector of relative weights associated with each variable. Weights will be estimated using the methodology chosen for the evaluation.<br/> Source: Program survey.</p> |
| <b>Component 3: Construction of cultural and athletic facilities</b>                           |                                      |        |        |        |        |  |  |
| <b>Outputs</b>   |                                      |        |        |        |        |  |  |
| Number of multipurpose courts/fields built   |                                      | 18     | 6      |        |        | 24   | Source: Program progress reports.  |
| <b>Outcomes</b>  |                                      |        |        |        |        |  |  |
| Students in beneficiary schools with access to recreational, cultural, and athletic facilities | 0                                    |        | 7,715  | 4,122  |        | 11,837   | Source: Program progress reports.  |
| Percentage of students reporting academic progress in beneficiary schools                      | To be determined at start of program |        |        |        |        | 5% improvement in academic progress index over baseline. | <p>Academic progress refers to decreased absenteeism and increased student participation in athletic, cultural, and extracurricular activities at school.<br/> Source: Program surveys</p>   |



## FIDUCIARY AGREEMENTS AND REQUIREMENTS

|                              |   |
|------------------------------|---|
| <b>Country:</b>              | Costa Rica  |
| <b>Project number/title:</b> | CR-L1053; Education Infrastructure Construction and Equipment   |
| <b>Executing agency:</b>     | Trustee banks subject to the supervision of the General Superintendency of Financial Entities (SUGEF), to be determined |
| <b>Prepared by:</b>          | Willy Bendix, Procurement Specialist (FMP/CR), and Andrés Suárez, Financial Management Specialist (FMP/CR)              |

### I. COUNTRY FIDUCIARY CONTEXT

- 1.1 The fiduciary evaluation was conducted on the basis of meetings with key personnel from the entities involved, the Bank-financed study on the diagnostic assessment of public works trusts, legal documentation on the concept of trusts, and meetings with the project team.
- 1.2 This operation will use an alternative, novel financing mechanism: a public works trust to finance and execute a public works project, which has already been used with autonomous Costa Rican entities.
- 1.3 The trust contract is governed by the Code of Commerce and also considers other possible sources of financing for the works, such as funds collected from investors in the securities market, as provided in the Law Regulating the Securities Market and related regulations. The Financial Administration Act of the Republic and Government Budgets, Law 8131 of 18 September 2001, restricts the establishment of trusts in the public sector by generally stating that trusts may not be established with treasury funds without a special law authorizing such trusts. Thus, the executor for the trust specifically established for this proposed operation will be determined after passage of the proposed law titled “Authorization for the Executive Branch to establish a trust and sign a public finance transaction through a long-term lease agreement to finance the MEP’s education infrastructure construction and equipment project throughout the country,” which was submitted by the MEP to the Legislative Assembly in September 2011.
- 1.4 As for procurement, Costa Rica has an extensive, hierarchically structured body of law (Constitution, laws, decrees, general regulations, and specific regulations). The Law on Administrative Contracting<sup>1</sup> governs the procurement and sale of goods and

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<sup>1</sup> Law 7494 of 16 May 2006.

services by all public enterprises and institutions comprising the State<sup>2</sup>; enshrines the principles<sup>3</sup> of equality and free competition, *inter alia*; and clearly defines procurement methods (competitive bidding, abbreviated tender, direct contracting, and others) as well as exceptions and general procedures. This law governs the content of bidding documents, requiring them to be appropriate, sufficient, and as neutral as possible, and states that rules on the reception and opening of bids must be clear and in accordance with best international practices.

- 1.5 Country financial systems were evaluated using the methodology of the Public Expenditure and Financial Accountability (PEFA) system, and Costa Rica's public finance management was found to be satisfactory overall in 2010. This report basically covered the expenses in the budget approved by the Legislative Assembly that are expenses of the central government. Using the treasury subsystem through a single window to make payments for Bank-financed projects reduces the major fiduciary risks in terms of payments, cash flow management, and reconciliations. In addition, public finances are reasonably well monitored by the Office of the Comptroller General.

## II. FIDUCIARY CONTEXT OF THE EXECUTING AGENCY

- 2.1 The executing unit will be attached to the trustee bank to be determined after passage of the law to finance the MEP's project to construct and equip education infrastructure throughout the country. In recent experiences, only State-owned commercial banks have acted as trustee banks, since their status as government entities allows other government entities to hire them directly without having to go through the ordinary administrative contracting procedures. Aside from the three State-owned commercial banks (Banco Nacional, Banco de Costa Rica, and Banco Crédito Agrícola de Cartago), the other financial institution that can fulfill that role under the same conditions is the Central American Bank for Economic Integration (CABEI).
- 2.2 The executing unit, either with its own staff or through a procurement agent, will be responsible for hiring the company that will carry out the projects and the company that will maintain the built infrastructure over the life of the trust, as well as for preparing the financial reports on the trust and the coordinated submittal of items requested by the Bank.

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<sup>2</sup> The ministries and entities under the central government, the Supreme Electoral Court, the Office of the Comptroller General, the Office of the Ombudsperson, the Utility Regulation Authority, decentralized entities, government supervision and control bodies, municipalities, public universities, nongovernmental public entities, public enterprises in which the State owns a 50% share or greater, or any other public entity and any contractual activity financed in whole or in part with public resources, regardless of the legal nature of the person or entity involved.

<sup>3</sup> In accordance with Articles 4 to 6 of the Law on Administrative Contracting, passed in 1996 and amended in 2009.

### III. ASSESSMENT OF FIDUCIARY RISK AND MITIGATION MEASURES

- 3.1 The recent regulations issued by the National Financial System Oversight Council require each trust to have its own executing unit to carry out planned activities through professionals or specialized firms, so that the trustee is not carrying out such activities directly. This executing unit may commission the services of a firm specializing in the type of specialized services needed, which decreases certain types of risk from the financial management standpoint, and the Bank will need to strengthen the professionals hired for this unit to execute externally financed projects in both procurement and financial matters. The MEP, as trustor, will participate in project development, execution, and supervision, ensuring that project requirements are fulfilled, and in particular will take cognizance of the reports and make the agreed lease payments on the predetermined dates, with the corresponding adjustments.<sup>4</sup> In addition, Decree 36450-H of the Office of the President sets forth the procedure for securing authorization for the financing of public works projects through securitization trusts, public works trusts, and other similar trusts with lease contracts, and this provides support for authorization of the trust in the Legislative Assembly.
- 3.2 In view of these circumstances and existing levels of control, this operation is deemed to be of medium fiduciary risk.

### IV. PROCUREMENT AGREEMENTS AND REQUIREMENTS

- 4.1 All procurement processes for works, goods, nonconsulting services, and consulting services must be included in the annual procurement plan previously approved by the Bank through the Procurement Plan Execution System and in accordance with the special stipulations of the loan contract.
- 4.2 **Procurement of works, goods, and nonconsulting services.** Contracts for works, goods, and nonconsulting services<sup>5</sup> generated under the project and subject to international competitive bidding (ICB) with geographic groupings will be executed using the Standard Bidding Documents issued by the Bank.
- 4.3 Procurement processes financed with local counterpart resources, such as those for technical and administrative personnel, operating and maintenance expenses, etc., if necessary, will be governed by local procedures provided that these are not in conflict with the principles established by the Bank. In such cases, the following must be verified: (i) strict compliance with applicable local laws; (ii) fulfillment of the program's objectives and technical requirements; (iii) satisfactory quality and compatibility with the rest of the project; (iv) timely delivery or completion; (v) pricing that does not have a negative effect on the project's economic and financial viability; and (vi) observance of the highest ethical standards.

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<sup>4</sup> As stated in the amendment to the Public Regulations on the Offering of Securities, National Financial System Oversight Council, in Article 8 of the minutes of session 881-2010 of 17 September 2010.

<sup>5</sup> In accordance with the Bank's procurement policies, nonconsulting services are treated as goods.

- 4.4 No contract for the procurement of goods, services, or works requires that contractors be prequalified. These procurement processes are listed in the initial procurement plan. The project's sector specialist is responsible for reviewing the technical specifications for the procurement of goods and works during the preparation of the bids. This specialist will also indicate whether outside support should be secured to help the executing agency evaluate the bids, in view of the nature and technical complexity of the procurement processes.
- 4.5 **Selection and contracting of consultants.** Contracts for consulting services generated under the project are listed in the procurement plan and will be executed using the Standard Request for Proposals issued by the Bank.
- a. **Selection of consulting firms.** The Bank-issued Standard Request for Proposals will be used for the project.
  - b. **Short list of consulting firms.**<sup>6</sup> This list may consist entirely (100%) of national firms<sup>7</sup> for contracts in amounts below the thresholds set by the Bank<sup>8</sup> for the country.
  - c. **Selection of individual consultants.** The qualifications of at least three candidates for the work will be compared.
- 4.6 The project's sector specialist is responsible for reviewing the terms of reference for the contracting of consulting services. The specialist will also indicate whether outside support should be secured to help the executing agency evaluate the bids, in view of the nature and technical complexity of the procurement processes. In some cases, the services of individual consultants may be requested through local or international advertising for the purpose of forming a short list of qualified individuals.
- 4.7 **Early procurement processes/retroactive financing.** In accordance with policy OP-504, recognition of expenses refers to the recognition, as part of the total project cost, of certain project-related payments made by the borrower before the Board of Executive Directors approves the loan or technical-cooperation operation, provided that such expenses or commitments stem from procurement processes that meet standards substantively comparable to those subsequently set forth in the loan contract. Early contracting refers to the obligations assumed by the borrower in relation to the procurement of goods, works, or services for project execution, before the Bank approves a loan or technical-cooperation operation.
- 4.8 **Procurement supervision.** Below is a summary of the procurement methods to be used in the proposed project.

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<sup>6</sup> In accordance with section V of the Policies for the Selection and Contracting of Consulting Services Financed by the Inter-American Development Bank, neither a short list nor the Standard Request for Proposals need be used in selecting individual consultants.

<sup>7</sup> Foreign firms are not barred from participating.

<sup>8</sup> VPC/PDP sets these thresholds.

**Table IV-1: Procurement method to be used based on the thresholds**

| Investment type   | Threshold (US\$000)                            | Procurement method  | Bank review method |
|---|--|---|--------------------|
| Works   | Equal to or greater than 3,000                 | ICB with geographic groupings   | Ex ante            |
|   | Less than 3,000                                | Shopping  | Ex post            |
| Goods and nonconsulting services  | Equal to or greater than 250                   | ICB with geographic groupings   | Ex ante            |
|   | Equal to or greater than 100 and less than 250 | National competitive bidding (NCB)  | Ex post            |
|   | Less than 100                                  | Shopping  | Ex post            |
| Consulting services (consulting firm)   | Equal to or greater than 200                   | Short list of six firms with broad geographic representation (international and national advertising) | Ex ante            |
|   | Less than 200                                  | Short list of six firms which may be national consultants (national advertising)                      | Ex post            |
| Consulting services (individual)  | Equal to or greater than 50                    | At least three candidates   | Ex ante            |
|   | Less than 50                                   |   | Ex post*           |
| Direct contracting of goods, works, nonconsulting services, and consulting services |  |   | Ex ante            |

\*The Bank may opt for ex ante supervision for any of these processes, such as for key personnel in the project executing unit.

## 1. Main procurement processes

| Category and description of procurement contract                                     | Type  | Total cost (US\$000) | Procurement method |
|--|-------|----------------------|--------------------|
| Construction of new buildings for 79 primary and secondary schools                   | Works | 155,000              | ICB                |
| Provision of furniture and equipment   | Goods | 3,000                | ICB                |
| Construction of multipurpose athletic facilities at 24 primary and secondary schools | Works | 9,500                | ICB                |

4.9 Bidding processes for goods and nonconsulting services will use the standard documents or those agreed upon with the Bank. Processes for selecting consulting services will use the Bank's Standard Request for Proposals.

4.10 In view of the foregoing, inspection visits to the executing agency should be carried out every six months for ex post reviews of procurement processes. The ex post review reports will include at least one physical inspection visit,<sup>9</sup> selected from among the procurement processes subject to ex post review (no less than 10% of all reviewed contracts should be physically inspected).

## V. AGREEMENTS AND REQUIREMENTS FOR FINANCIAL MANAGEMENT

### 1. Disbursements and cash flow

5.1 The trust is expected to administer proceeds from the Bank loan. Disbursements of proceeds from the loan will be subject to the financial plan requirements of the three phases established for project financing. The executing unit must explicitly

<sup>9</sup> The inspection verifies the existence of the items procured, while the sector specialist verifies quality and fulfillment of specifications.

state the disbursement amounts it is requesting based on the specific needs of each phase for at least 180 days, and these disbursements should be in accordance with a projection based on the activities in the approved procurement plan. For the trustee to use the funds, a separate individual bank account will be opened in the centralized government treasury account, so that resources may be disbursed to this account and administered by the trustee bank selected.

## **2. Accounting and internal control**

- 5.2 The trust for financing the MEP's education infrastructure construction and equipment project is governed by the Regulations on the Public Offering of Securities for Trusts, by the provisions established primarily by the National Financial System Oversight Council, which in turn delegates the authority to oversee this instrument to the SUGEF. It also features the participation and oversight of the MEP in its capacity as trustor, to ensure that the contract's requirements are satisfactorily met.
- 5.3 As for the executing agency's internal controls, the executing agency must have a functional structure including matters related to accounting records, finances, and other policies and procedures governing the trust and, in particular, the executing unit. Operating regulations will need to be developed for execution, and they should clearly state who is responsible for formulating and approving policies and procedures, as well as providing details on financial execution and required reporting, *inter alia*.
- 5.4 The executing unit will submit to the oversight committee and the trustee the project status reports on construction and equipment, as well as budgetary, technical, financial, and other matters deemed relevant. The trustee will forward the reports to the MEP for approval.
- 5.5 For financial reports and statements, the financial statements on trust assets will be requested on the basis of International Financial Reporting Standards, as is customary for trustee banks, supplemented by the investment statement for program components.

## **3. External auditing**

- 5.6 The executing unit will submit an audited report on the trust, annually and at the end of the project, based on the financial statements that the executing unit will need to maintain showing the sources and uses of funds. These reports will show the revenues from the Bank, the counterpart, the execution of investment categories, the explanatory notes describing the accounting policies used, and a report on reconciliation of the bank account at the end of each fiscal year. These audited reports must be submitted within 120 days after the end of the year (31 December), and the final report must be submitted within 120 days after the last disbursement, in accordance with policy OP-273. Thus, the executing agency must ensure that the funds for auditing services are available and have been budgeted up to the end of the project.

- 5.7 The report will contain the auditors' opinion, providing further details on the eligibility of each expense and showing that the expenses paid for with Bank funds were in accordance with the purposes specified in the loan contract. The commissioning and scope of these audits will be in accordance with the terms of reference agreed upon between the executing unit and the Bank. The total cost of these audits will be financed with Bank resources.

#### **4. Exchange rate**

- 5.8 The inclusion of the Central Bank's benchmark sell rate on the date on which the borrower makes the respective payments in local currency for transfer into the currency of the operation is recommended.

#### **5. Financial supervision plan**

- 5.9 The information supporting the justification of expenses will be reviewed after the Bank's resources have been disbursed. In view of the medium level of financial risk, reviews of the supporting documents for disbursement requests will be conducted at least every six months. During the fiduciary supervision visit to the executing unit in the selected trustee bank, and depending on the outcome of the ex post review of disbursements, a change in the frequency of the fiduciary visits may be considered if necessary.
- 5.10 Audits will be performed annually, and the final audit will include an opinion on the statement of revenues and expenses, including the items mentioned in the specific section. The Bank will provide continuous training in ex post reviews and disbursement processes for the personnel in charge of the finances and procurement processes for the executing agency and will recommend effective maintenance of appropriate internal controls.

#### **6. Execution mechanism**

- 5.11 The MEP, through a Project Supervision Unit, will be the technical counterpart of the executing unit to be established by the trust. The MEP or trustor will be the beneficiary of the infrastructure that is built. As part of its contributions to the trust, the MEP will grant the right to use some plots of land for the construction of education infrastructure and will furnish the prototypical designs (developed by the Office of Education Infrastructure and Equipment) to be used as the basis for the specific design of each project. The central government will have the obligation of making a lease payment for the works received throughout the life of the trust.

DOCUMENT OF THE INTER-AMERICAN DEVELOPMENT BANK

PROPOSED RESOLUTION DE-\_\_\_/12

Costa Rica. Loan \_\_\_\_/OC-CR to a trust to be set up by the Republic of Costa Rica,  
as represented by a Costa Rican public bank to be selected as trustee  
or its successors, replacements or substitutes as trustee  
Education Infrastructure Construction and Equipment

The Board of Executive Directors

RESOLVES:

That the President of the Bank, or such representative as he shall designate, is authorized, in the name and on behalf of the Bank, to enter into such contract or contracts as may be necessary with a trust to be set up by the Republic of Costa Rica under the Costa Rican laws as represented by a Costa Rican public bank to be selected as trustee or its successors, replacements or substitutes as trustee, as Borrower, and with the Republic of Costa Rica, as Guarantor, for the purpose of granting the former a financing to cooperate in the execution of an education infrastructure construction and equipment program. Such financing will be for the amount of up to US\$167,000,000, from the resources of the Bank's Ordinary Capital, and will be subject to the Financial Terms and Conditions and the Special Contractual Conditions of the Project Summary of the Loan Proposal.

(Adopted on \_\_ \_\_\_\_\_ 2012)