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The World Bank

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Report No: 63918-BR

PROJECT APPRAISAL DOCUMENT

ON A

PROPOSED LOAN

IN THE AMOUNT OF

US$130 MILLION

TO THE

MUNICIPALITY OF RECIFE

WITH A GUARANTEE FROM THE FEDERATIVE REPUBLIC OF BRAZIL

FOR THE

RECIFE EDUCATION AND PUBLIC MANAGEMENT PROJECT
(PROGRAMA DE DESENVOLVIMENTO DA EDUCAÇÃO E DA GESTÃO PÚBLICA NO MUNICÍPIO DO RECIFE)

April 26, 2012

Human Development Sector
Brazil Country Management Unit
Latin American and the Caribbean Regional Office

CURRENCY EQUIVALENTS
(Exchange Rate Effective September 30, 2011)

Currency Unit	=	Brazilian Reais
BRL 1.8536	=	US$1
US$0.5395	=	BRL 1

FISCAL YEAR
January 1 – December 31

ABBREVIATIONS AND ACRONYMS

CQS	Selection Based on Consultants' Qualifications
CGM	General Comptroller's Office (*Controladoria Geral do Município*)
CMEIs	Municipal Early Child Education Centers (*Centro Municipal de Educação Infantil*)
COMUDE	Municipal Conference on Education (*Conferência Municipal de Educação*)
CSO	Civil Society Organization *(Organização da Sociedade Civil)*
CTTU	Company of Urban Transport and Traffic *(Companhia de Trânsito e Transporte Urbano)*
DA	Designated Account
DLI	Disbursement-linked Indicator
ECD	Early Child Development
ECE	Early Child Education
EEP	Eligible Expenditure Program
EMF	Environmental Management Framework
EMPREL	Municipal Information Technology Company (*Empresa Municipal de Informática*)
FBS	Fixed Budget Selection
FM	Financial Management
FPM	Municipalities' Participation Fund *(Fundo de Participação dos Municípios)*
FUNDEB	Fund for the Maintenance and Development of Basic Education and of the Education Professionals' Valorization *(Fundo de Manutenção e Desenvolvimento da Educação Básica e da Valorização dos Profissionais da Educação)*
FUNDEF	Fund for the Maintenance and Development of Fundamental Education and of the Teachers' Valorization *(Fundo de Manutenção e Desenvolvimento do Ensino Fundamental e da Valorização dos Professores)*
GDP	Gross Domestic Product
IBGE	Federal Bureau of Statistics *(Instituto Brasileiro de Geografia e Estatísticas)*
ICB	International Competitive Bidding
ICMS	Trading and Suppliers Service Tax *(Imposto sobre Circulação de Mercadorias e Prestação de Serviços)*

IDB	Inter-American Development Bank
IFR	Interim Financial Report
INSS	Social Security National Institute *(Instituto Nacional do Seguro Social)*
IPCA	Consumer Price Index *(Indice Nacional de Preços ao Consumidor Amplo)*
IPTU	Urban Land and Property Tax *(Imposto Predial e Territorial Urbano)*
IQE	Institute for Quality Teaching *(Instituto de Qualidade da Educação)*
ISS	Tax on Services *(Imposto sobre Serviços)*
IVA	Independent Verification Agency
LCS	Least-Cost Selection
LCSHE	Latin America and the Caribbean Education Sector
LDO	Law of Budget Guidelines (*Lei de Diretrizes Orçamentárias*)
LOA	Annual Budget Law (*Lei Orçamentária Anual*)
MOP	Project Operational Manual
MOR	Municipality of Recife (*Município do Recife*)
MTR	Mid-term Review
NCB	National Competitive Bidding
NCR	Net Current Revenue
PDO	Project Development Objective
PIM	Better Early Childhood Program (*Programa Primeira Infância Melhor*)
PIU	Project Implementation Unit
PPA	Multi-Year Plan *(Plano Plurianual)*
QBS	Quality-Based Selection
QCBS	Quality- and Cost-Based Selection
RECIPREV	Recife's Pension Fund *(Regime Próprio de Previdência Social do Município do Recife)*
RMR	Recife Metropolitan Region (*Região Metropolitana de Recife*)
SAEPE	Pernambuco Student Assessment System *(Sistema de Avaliação Educacional de Pernambuco)*
SADGP	Secretariat of Public Administration and Personnel Management (*Secretaria de Administração e Gestão de Pessoas*)
SAJ	Secretariat of Legal Affairs (*Secretaria de Assuntos Jurídicos*)
SBD	Standard Bidding Documents
SEI	Integrated Structural System (*Sistema Estrutural Integrado*)
SEEL	Secretariat of Education *(Secretaria de Educação, Esporte e Lazer)*
SEFIN	Secretariat of Finance *(Secretaria de Finanças)*
SEGESP	Special Secretariat of Management and Planning *(Secretaria Especial de Gestão e Planejamento)*
SMAR	Municipal System of Student Assessment *(Sistema Municipal de Avaliação da Rede)*
SOE	Statement of Expenditures
SOFIN	Public Financial Management System (*Sistema Orçamentário e Financeiro*)
SSP	Secretariat of Public Services *(Secretaria de Serviços Públicos)*

STN	National Treasury *(Secretaria do Tesouro Nacional)*
SUS	Unified Health System *(Sistema Único de Saúde)*
SWAp	Sector-Wide Approach
TOR	Terms of Reference
URB	Recife Urbanization Company (*Empresa de Urbanização do Recife*)

Regional Vice President:	Hasan A. Tuluy
Country Director:	Deborah L. Wetzel
Sector Director:	Keith Hansen
Sector Manager:	Chingboon Lee
Task Team Leaders:	David Evans and Daniela Pena de Lima

FEDERATIVE REPUBLIC OF BRAZIL
Recife Education and Public Management Project
(Programa de Desenvolvimento da Educação e da Gestão Pública no Município do Recife)

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PAD DATA SHEET

Federative Republic of Brazil

Recife Education and Public Management Project
(Programa de Desenvolvimento da Educação e da Gestão Pública no Município do Recife)

PROJECT APPRAISAL DOCUMENT

Latin America and the Caribbean Region

LCSHE

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Basic Information

Date:	April 26, 2012	Sectors:	Pre-primary education (40%); Primary education (40%); Public administration- Other social services (8%); General finance sector (8%); General transportation sector (4%)
Country Director:	Deborah L. Wetzel	Themes:	Education for all (80%); Other public sector governance (20%)
Sector Manager/Director:	Chingboon Lee/Keith Hansen	EA Category:	B - Partial Assessment
Project ID:	P126372		
Lending Instrument:	Specific Investment Loan		
Team Leader(s):	David Evans/Daniela Pena de Lima		

Joint IFC: No

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Borrower: Municipality of Recife

Responsible Agency: Special Secretariat of Planning and Management (SEGESP)
Cais do Apolo, 925 9 andar
50030-903 Recife PE, Brazil

Contact:	Evelyne Labanca Corrêa de Araújo	Title:	Secretary
Telephone No. Fax:	(55 81) 3355-9444 (55-81) 3355-8014	Email:	elabanca@recife.pe.gov.br

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Project Implementation Period:	Start Date: September 3, 2012	End Date:	October 31, 2017
Expected Effectiveness Date:	September 3, 2012		
Expected Closing Date:	April 30, 2018		
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Project Financing Data(US$M)		
[x] Loan	[ ] Grant	[ ] Other
[ ] Credit	[ ] Guarantee	

For Loans/Credits/Others			
Total Project Cost :	921.60	Total Bank Financing :	130.0
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Financing Source	**Amount(US$M)**
BORROWER/RECIPIENT	791.6
IBRD	130.0
Total	921.6
.	

Expected Disbursements (in USD Million)

Fiscal Year	**13**	**14**	**15**	**16**	**17**	**18**
Annual	31.6	19.9	25.3	25.9	21.6	5.7
Cumulative	31.6	51.5	76.8	102.7	124.3	130.0

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Project Development Objective(s)

The objective of the Project is to expand coverage of improved early child education (ECD), create conditions more conducive to learning in fundamental education, and improve municipal public management, all within the Borrower's territory.

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Components

Component Name	**Cost (USD Millions)**	
Component 1: Expand coverage of improved ECD and create conditions conducive to learning in fundamental education	Estimated total cost: Bank:	US$891.6 US$100.0
Component 2: Strengthen institutions for more efficient and effective public management	Estimated total cost: Bank:	US$30.0 US$30.0

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Compliance	
Policy	
Does the project depart from the CAS in content or in other significant respects?	Yes [ ] No [x]

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Does the project require any waivers of Bank policies?	Yes [ ] No [x]
Have these been approved by Bank management?	Yes [ ] No [ ]
Is approval for any policy waiver sought from the Board?	Yes [ ] No [ ]
Does the project meet the Regional criteria for readiness for implementation?	Yes [x] No [ ]

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Safeguard Policies Triggered by the Project	**Yes**	**No**
Environmental Assessment OP/BP 4.01	X	
Natural Habitats OP/BP 4.04		X
Forests OP/BP 4.36		X
Pest Management OP 4.09		X
Physical Cultural Resources OP/BP 4.11		X
Indigenous Peoples OP/BP 4.10		X
Involuntary Resettlement OP/BP 4.12		X
Safety of Dams OP/BP 4.37		X
Projects on International Waterways OP/BP 7.50		X
Projects in Disputed Areas OP/BP 7.60		X

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Legal Covenants

Name	**Recurrent**	**Due Date**	**Frequency**
Institutional Arrangements. Schedule 2. Section I.A.1.(a)	Yes	No later than 2 months after effectiveness	Semi-annual

Description of Covenant

The Municipality of Recife (MOR) shall create and thereafter maintain, until completion of the execution of the Project, an implementation unit within SEGESP, to be responsible for the overall implementation of the Project (the "PIU"). Such unit shall have staff in adequate numbers and with qualifications and experience satisfactory to the Bank including a Project coordinator, a deputy coordinator, a procurement specialist, a financial management specialist, and other personnel needed for the effective implementation of the Project, all as set forth in the Project Operational Manual (MOP).

Name	**Recurrent**	**Due Date**	**Frequency**
Institutional Arrangements. Schedule 2. Section I.A.1.(b)		No later than 2 months	Annual

		after effectiveness	

Description of Covenant
The MOR shall create and thereafter maintain, until completion of the execution of the Project, a Project Consultative Committee, responsible for overseeing implementation, monitoring and evaluation of all Project activities and provide recommendations based on review of progress reports and other relevant documents prepared for the Project, and with structure and functions satisfactory to the Bank, as set forth in the MOP.

Name	**Recurrent**	**Due Date**	**Frequency**
Implementation Arrangements. Schedule 2. Section I.B.4.	Yes	Ongoing	Annual

Description of Covenant
The MOR shall ensure that the budget code number indicated in the EEP table shall conform to the MOR's annual budget law. The MOR and the Bank agree that such budget code number may change under the MOR's budget law provided, however, that there is no change in the corresponding EEP and in the underlying activities to be financed by the Bank under such EEP.

Name	**Recurrent**	**Due Date**	**Frequency**
Implementation Arrangements. Schedule 2. Section I.B.5.	Yes	Ongoing	Annual

Description of Covenant
The MOR, though SEGESP, and the Bank may jointly adjust, once every year, the amounts assigned per budget code to the EEPs, in a manner satisfactory to the Bank.

Name	**Recurrent**	**Due Date**	**Frequency**
Safeguards. Schedule 2. Section I.D.1.	Yes	Ongoing	Annual

Description of Covenant
The MOR shall, with the assistance of the pertinent participating entity, implement the Project in accordance with the provisions of the Environmental Management Framework (EMF) and those of each environmental management plan required as per the terms of the EMF, prepared by the MOR and approved by the Bank.

Name	**Recurrent**	**Due Date**	**Frequency**
Implementation Arrangements. Schedule 2. Section I.B.6.	No	Mid-way through Project	Once

Description of Covenant
Prior to the sixth disbursement under Category (1), the MOR shall (i) carry out a mid-term review with the Bank on the overall progress in the execution of the Project and on the accomplishment of the Project, (ii) review whether adjustments or replacement of the existing DLIs are needed, and (iii) thereafter make the required adjustments, all in a manner acceptable to the Bank.

Name	**Recurrent**	**Due Date**	**Frequency**
Project Monitoring. Schedule 2. Section II.A.3.	Yes	18 months after project effectiveness	At least twice

Description of Covenant
The MOR shall select and contract an entity, independent from the MOR (Independent Verification Agency – IVA) with experience and qualifications in education acceptable to the Bank. The IVA should be responsible

for carrying out at least two (2) technical audits during the Project, particularly focused on compliance with the DLIs; (b) furnish to the Bank as soon as available, but in any case not later than the sixth Loan withdrawal and the eleventh Loan withdrawal, respectively, the two audit reports of the Independent Verification Agency of scope and detail as the Bank shall have reasonably requested; and (c) furnish to the Bank such other information concerning said technical audits and documentation as the Bank shall from time to time reasonably request.

Team Composition

Bank Staff

Name	Title	Specialization	Unit	UPI
David Evans	Senior Economist,	Co-TTL	LCSHE	213993
Daniela Pena de Lima	Senior Operations Officer	Co-TTL	LCSHH	98726
Jose M. Rodriguez Alvarez	Senior Public Sector Specialist	Public Management	LCSPS	210245
Mariano Lafuente	Public Sector Management Specialist	Public Management	LCSPS	207610
Tarsila Velloso	Public Sector Management Specialist	Public Management	LCSPS	342867
Susana Amaral	Financial Management Specialist	Financial Management	LCSFM	71475
Sinue Aliram	Procurement Specialist	Procurement	LCSPT	235731
Catarina Isabel Portelo	Senior Counsel,	Lawyer	LEGLA	221750
Marta Molares-Halberg	Lead Counsel	Lawyer	LEGLA	13064
Janet K. Entwistle	Senior Operations Officer	Operations	LCSHE	13739
Miguel-Santiago Oliveira	Senior Finance Officer	Loan Officer/ Disbursement	CTRLN	260058
Victor Ordonez	Finance Officer,	Loan Officer/ Disbursement	CTRLN	178705
Gunars Platais	Senior Environmental Economist	Safeguards/Environment	LCSEN	73535
Sarah Keener	Senior Social Development Specialist	Safeguards/Social	LCSSO	22949
Carla Zardo	Program Assistant,	Team Assistant	LCC5C	87301
Maria Colchao	Senior Program Assistant	Operations	LCSHH	76627
Non Bank Staff				
Erica Amorim	Consultant	Education	LCSHE	256767

Maria Madalena dos Santos	Consultant	Education	LCSHH	55141
Ricardo Marar	Consultant	Transport	LCSHE	368559
Sol Garson	Consultant	Economist	LCSPE	214794
Rafael Barroso	Consultant	Economist/Financial Sector	LCSPE	377165
Laudo Bernardes	Consultant	Institutional Arrangements and Project Operational Manual	LCSHE	63344

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Locations

Country	First Administrative Division	Location	Planned	Actual	Comments
Brazil	Municipality	MOR			

I. Strategic Context

A. Country Context

1. The Municipality of Recife (*Município do Recife* -- MOR), capital of the State of Pernambuco, has the second highest unemployment rate of any metropolitan area in the country. With 28 percent of its almost 471,000 households (and 1.5 million inhabitants) earning under R$830 (US$448) per month, the Recife Metropolitan Region (RMR) is the second poorest of any metropolitan area. It is by far the largest municipality in RMR, which is the sixth largest metropolitan region in the country. It is on the northeast coast of Brazil, centrally located between two other regional centers, Salvador and Fortaleza.

2. Recife's population has grown by 12.5 percent over the last ten years. The nature of the economy continues to evolve, with the vast majority (83 percent) of the Recife economy now focused in the service sector. As the state capital, Recife needs a flexible workforce resulting from a quality education – beginning from an effective foundation in early child education – and an efficient public management system to provide that education. The growth has led to increased traffic problems and highlighted weaknesses in managing urban mobility, which are expected to worsen in the absence of significant policy changes.

B. Sectoral and Institutional Context

Education

3. In Brazil, the principal responsibilities of the municipal education system are early child education (ECE) and fundamental education (primary and lower secondary, consisting of 9 years, from age 6 to age 14), as well as adult education, for which responsibilities are shared with the states. According to the 2010 School Census, there are just over 46,000 children age 0-5 enrolled in ECE in Recife, of which 34 percent are in municipal centers and another 20 percent are in municipally contracted private centers. Almost all of the rest are in private centers with no link to government. At the fundamental education level, 219,335 children are enrolled, with 34 percent in the municipal system. An equal number (34 percent) are enrolled in the state system, with slightly fewer (32 percent) in private institutions. Due to various legal reforms,[1] the municipal education system would gradually absorb the entire fundamental education population, doubling its enrollment in coming years and demanding greater management capacity.

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[1] The 1988 Constitution established the legal framework for the decentralization of fundamental education to municipalities, which was later complemented by the education finance funds - Fund for the Maintenance and Development of Fundamental Education and of the Teachers' Valorization *(Fundo de Manutenção e Desenvolvimento do Ensino Fundamental e da Valorização dos Professores* – FUNDEF, 1996) and Fund for the Maintenance and Development of Basic Education and of the Education Professionals' Valorization *(Fundo de Manutenção e Desenvolvimento da Educação Básica e da Valorização dos Profissionais da* Educação – FUNDEB, 2007), which created incentives for municipalities to enroll students in fundamental education.

4. Recife lags behind both the region and the country in early child education. *Creche* (daycare centers, 0-3 year olds) coverage is 12 percent of the 0-3 year old population in Recife, with just 7 percent of coverage provided in municipal *creches*. This is well below the 18 percent average coverage of the nation as a whole and even the almost 16 percent coverage of the northeastern region. Coverage at the pre-school level (age 4-5), which is now constitutionally obligatory, is 80 percent. This is slightly higher than the nation but still trails the northeastern region. Furthermore, early child education enrollments have risen relatively little over the last decade, from almost 13,000 children in 1999 to just below 16,000 in 2010. That growth rate of 22 percent is less than half the growth rate for the nation as a whole. As such, expanding coverage is a high priority for the MOR.

5. The low ECE coverage is mainly caused by the dual problems of insufficient centers and existing centers with unsatisfactory infrastructure conditions to qualify for federal funds for expansion. There are 75 publicly funded ECE centers for children age 0 to 5: 50 owned by the MOR, 6 rented, and 19 contracted from non-profit providers. Two comparably sized municipalities, Fortaleza and Teresina, have 270 and 130 *creches* and pre-schools, respectively. Most of these facilities were not planned or designed to function as ECE centers: some lack facilities such as playgrounds, meal rooms and libraries, others have insufficient classroom size, and some have bathrooms not adapted to young children.

6. Early child development (ECD) programs have great potential to compensate for inequalities in income and background. An effective ECD program requires the engagement of other secretariats such as social assistance and health. At present, there is insufficient articulation of early child services across sectors in Recife, although programs elsewhere in Brazil have shown how coordinated services can be effective. One successful multi-sectoral ECD program in Brazil is in Rio Grande do Sul: Better Early Childhood Program (*Programa Primeira Infância Melhor* -- PIM). Early evidence from an evaluation of PIM demonstrates significant gains for children in cognitive, social, and motor development.

7. Quality of fundamental education in Recife is weak. Student performance on national and state examinations is extremely low. Results from 2005 to 2009 on the national standardized test that assesses grades 5 and 9 (*Prova Brasil)* showed that Recife seriously underperforms relative to its peers. In Year 5, Recife ranked among the bottom three state capitals in both mathematics and Portuguese. In Year 9, Recife ranked last in both areas.

8. A key factor in the low performance of Recife's fundamental school students is high age-grade distortion rates. Forty-three percent of students in the late years of fundamental education in Recife are old for their grade; 20 percent of students in early years of fundamental education suffer the same problem. This age-grade distortion is one of the major causes of Recife's low student learning performance and drop-out rates mainly in the late years of fundamental education, as children are increasingly drawn to work opportunities. Age-grade distortion is both a symptom (of low learning and potentially inefficient rules about student advancement) and a problem (in that students are drawn away from school without learning basic skills). While more general quality improvements are likely to reduce future incidence of this problem, more targeted interventions are necessary to deal with the immediate stock of over-age students at risk of drop-out.

9. A second factor in Recife's low performance is high rates of illiteracy in the early years of primary school. The most recent national standardized test for younger students (*Provinha Brasil)* showed that less than half of the students (42 percent) in the second year of school are literate. The state standardized test results showed that only 55 percent of students in the third year are literate. Without this basic foundation of early grade literacy, it is impossible for children to achieve a quality education later.

10. A third factor in Recife's low performance is teacher quality. The MOR has identified teacher quality as a significant challenge and is investing in new and innovative teacher training programs, which include in-class follow-up by trainers. Although precise data are difficult to come by, classroom observations in Pernambuco schools revealed that teachers spent less time on teaching activities (as opposed to classroom organization and other non-academic activities) than in either the state of Minas Gerais or the municipality of Rio de Janeiro. Teacher training has the potential to both increase time spent on academic activities and improve the quality of that time.

11. The current, short school day limits students' opportunities to advance academically. Extensive research has demonstrated the importance of sufficient academic learning time and the effective use of that time for improving student performance.[2] The school day in Recife is currently only four hours, and this fails to take advantage of available hours to help low-performing students improve.

Public Management

12. Underlying the effective functioning of the education system and other public services is the efficiency of the public sector. The tax system is a key factor in stabilizing and augmenting funding for these services. More than half of public resources (55 percent) derive from federal and state transfers, leading Recife's revenues to be subject to instability at these higher levels of government. Actual tax collection is far from its potential, which leaves ample room to increase tax revenue by more efficiently capitalizing on the existing tax base. As in many big cities in Brazil (and around the world), services are a major and fast growing economic activity. In Recife, services accounted for 80 percent of GDP in 2009. Taxes on Services (*Imposto sobre Serviços* -- ISS) were responsible for more than 47 percent of total tax revenues in 2011. The ISS tax management has been modernized, with the adoption of the electronic fiscal note system, but coverage is still limited to major taxpayers. Urban Land and Property tax (*Imposto Predial e Territorial Urbano* -- IPTU) administration presents more serious challenges. Partially due to increased economic activity, Recife's IPTU revenues decreased as a percentage of total local tax revenues between 2003 and 2011. While property tax revenues did increase about 21 percent in real terms in the period 2006-11, this was achieved with no relevant initiatives on tax administration. Even though the MOR experienced major growth in the number of properties and their market values, the latest revision of property registers occurred in 1997 and covered only 60 percent of properties. Many of the properties built with the expansion of the city in the last

[2] See Fisher *et al*, "Teaching Behaviors, Academic Learning Time, and Student Achievement: An Overview," Journal of Classroom Interaction 17(1), 1981, or Stallings J, "Allocated Academic Learning Time Revisited, or Beyond Time on Task," Educational Researcher 9(11), 1980.

decade have not yet been included in the cadastre. It is also crucial to carry out a complete property reassessment in the city. In addition, according to the municipal office responsible for tax collection, no report is regularly produced on any municipal tax. The MOR does not have a system to register and follow up on non-tax revenues (fines and fees, among other sources), thereby losing potential income. Online tax collection represents less than one percent of the total.

13. Management of the municipal debt also requires significant reform. Certain types of municipal debt – indirect administration bank debt, for example – are not even recorded by the Secretariat of Finance (*Secretaria de Finanças* -- SEFIN). Even after 2001-03, when the Social Security National Institute (*Instituto Nacional do Seguro Social* -- INSS) made a statement of debts in arrears and the MOR began to renegotiate, no controls were set to avoid new liabilities. Needed reforms are not limited to outstanding debt control, but include servicing of the debt. Rescheduling of INSS debt, which represents 85 percent of outstanding debt, led to changes in the methodology of debt servicing, but initiatives are needed to clarify the correct amount the MOR must pay from year to year.

14. Increasing the efficiency and quality of public expenditures would require improved control over the payroll and strengthening Recife's public financial management and procurement capacity. Personnel expenditures represented 42 percent of total expenditures in 2011, and there is no consolidated control over the number of public servants. Recife's public servants payroll is partially manual, unnecessarily complex (including a large number of allowances), and lacks the minimum controls needed to ensure the right remunerations are paid to the right people. Improved policies are likewise needed to attract and retain skilled personnel. Compliance with national accounting standards mandated for the coming years would require strengthening SEFIN's accounting unit, and the procurement unit's capacity would need to be enhanced.

15. The link between planning and budgeting is weak. Despite efforts to improve political and managerial monitoring of the Multi-Year Plan (*Plano Plurianual* -- PPA) implementation, Recife still does not have a results-based management system linking planning and budgeting, and the connection between these crucial policy tools is weak. The MOR has expressed a strong interest in improving the implementation of the PPA and its coherence with the budget. Program monitoring and evaluation needs to be strengthened and management processes need to be simplified. The Special Secretariat of Management and Planning (*Secretaria Especial de Gestão e Planejamento* -- SEGESP) has improved 15 key management processes and is planning to expand this to municipal administrative procedures.[3]

16. Urban mobility management is a challenge. In Recife, over the decades, rapid urbanization has resulted in uncontrolled urban sprawl with associated traffic congestion and increasing travel distances. The problems and costs of traffic congestion in Recife contribute negatively to the economic development and competitiveness prospects of the region and tend to

[3] Improved management processes included: fiscal notification and procurement (SEFIN), retirement (Secretariat of Public Administration and Personnel Management -- SADGP), publication of the official gazette (Secretariat of Communications) and strategic project management, environmental permits and construction permits (Recife Urbanization Company -- URB), among other.

have a disproportionate impact on the poor who are more likely to live far from their place of employment. Elsewhere, these mobility problems have been demonstrated to lead to exclusion from educational services.[4] The 2011 Recife Municipal Plan for Mobility stresses the need for specific studies to justify and implement established guidelines to improve the situation.

C. Higher Level Objectives to which the Project Contributes

17. The World Bank's Group Country Partnership Strategy FY2012-2015 (Report #63731-BR), discussed by the Executive Directors on November 1, 2011, emphasizes improving access to quality education, reducing age-grade distortion, and increasing the effectiveness of public management. It highlights the high returns to early child development. Furthermore, the current Brazilian administration has emphasized the importance of early child development as one of its key areas of focus. The Country Partnership Strategy also places emphasis on public management effectiveness and results-oriented public sector reforms, both areas included in this operation.

II. Project Development Objectives

A. PDO

18. The objective of the Project is to expand coverage of improved early child education (ECE), create conditions more conducive to learning in fundamental education, and improve municipal public management, all within the MOR's territory.

Project Beneficiaries

19. The Project has several groups of beneficiaries. The first is the children age 0-5 who would benefit from the upgrading of infrastructure for early child education, and the multi-sectoral coordination of services at that level. The second is the children in primary and lower secondary school who would benefit from the improved conditions for learning in fundamental education. Third, the beneficiaries of public management improvements would be the municipal administration, taxpayers, public servants, teachers, and users of local services.

PDO Level Results Indicators

20. Achievement of the PDO would be measured through the following five PDO level results indicators: (a) Number of children enrolled in the multi-sectoral early child development program, (b) proportion of students successfully exiting accelerated learning programs, (c) number of students enrolled in extended school day program, (d) IPTU revenues increase in real terms; and (e) improved municipal management through a more efficient administration and stronger control on payroll, leading to savings on personnel expenditures.

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[4] Susan Kenyon, "Transport and social exclusion: access to higher education in the UK policy context", Social Research in Transport (SORT) Clearinghouse, 2010.

III. Project Description

A. Project Components

21. The Project would have two components, the first of which would provide support for the implementation of the Eligible Expenditure Programs (EEP), and the second of which would provide technical assistance to strengthen the MOR's public management.

22. **Component 1: Expand coverage of improved ECE and create conditions conducive to learning in fundamental education** ***(Estimated total cost: US$891.6 million; Bank: US$100.0 million).***[5] This component would provide support for the implementation of the Eligible Expenditure Programs (EEPs), including activities to: (i) rehabilitate ECE centers; (ii) promote multi-sectoral early child development; (iii) create conditions more conducive to learning in fundamental education; (iv) professional development of the municipal teaching force; and (v) education management.[6]

23. ***Sub-Component 1(a):*** **Rehabilitate ECE centers including *creches*, preschools and Municipal Early Child Education Centers (*Centros Municipais de Educação Infantil* -- CMEIs), which combine *creche* and pre-school provision.** The Project would support emergency and priority rehabilitation on up to 75 early child education centers, representing the MOR's entire ECE network, consisting of 54 creches, 10 pre-schools, and 11 CMEIs. In 2011, the education engineering team developed a taxonomy of emergency, priority, and other rehabilitation needs, with the goal of providing emergency rehabilitation in all ECE centers and priority rehabilitation in the vast majority of ECE centers. At the beginning of each calendar year, ECE center directors report needed rehabilitation. The MOR would then prioritize these needs systematically, based on the new framework, and carry out 100 percent of emergency rehabilitation and at least 80 percent of priority rehabilitation requests.

24. ***Sub-Component 1(b): Promote multi-sectoral early child development***. The Project would support the pilot implementation of a program to provide individualized attention with a multi-sectoral focus. Based on the multi-sectoral PIM in Rio Grande do Sul, this pilot would offer services to children age 0-5 and their families. The program would be piloted in Region 4 of the MOR, which consists of twelve neighborhoods and – pending success in that area – would serve as a base for expansion throughout the MOR. The Project would include implementation of a program of home visits and monitoring of children age 0 to 5 and their families, as well as educational activities for children in schools and visits to other public facilities such as museums, theaters, and parks. It would also include the articulation of unified policies by varied secretariats (education, health, social assistance), and the stimulation of best practices for development at this age.

[5] Estimated total cost includes baseline costs, price contingencies, physical contingencies, and the front end fee, which the MOR will pay upfront from own resources, which explains the difference from the Component 1 cost excluding those costs (US$762,543,080) listed in Table 2 below.

[6] Given that the Bank is financing only a part of the Government's priority expenditure programs in this component and the SWAp mechanism allows flexibility in the allocation of funds across sub-components, this document does not specify the exact amount of financing associated with each sub-component. The exact allocation would be defined during implementation of the Project as the MOR submits eligible expenditures to be financed.

25. ***Sub-Component 1(c): Create conditions more conducive to learning in fundamental education***. This would be achieved through provision of support to create conditions more conducive to learning in fundamental education, including: (i) extension of the school day with two additional hours of focused education in mathematics and Portuguese; (ii) support of a program to improve attendance for vulnerable students (School Grant, or *Bolsa Escola*), and (iii) support of two early-grade accelerated learning programs, Get Focused and Accelerate Brazil (*Se Liga* and *Acelera Brasil*).

26. The Project would support the extension of the school day by two hours, focused on children with learning delays. Extensive research has demonstrated the importance of sufficient academic learning time and the effective use of that time for improving student performance. Furthermore, the State of Pernambuco has implemented full-day schooling in many of its secondary schools, resulting in the best test score results in the entire system. The MOR program is an expansion of a pilot program carried out in 2007 and 2008, called Literacy Teacher (*Professor Alfabetizador*). The Secretariat of Education *(Secretaria de Educação, Esporte e Lazer* -- SEEL) has identified 7,789 students in the third year of fundamental education (58 percent of all students in that year) and 8,452 students in the fifth year (74 percent of all students) with learning delays, according to state testing data. The Federal University at Pernambuco (*Universidade Federal de Pernambuco* -- UFPE), which partnered with the MOR on the 2007-08 pilot, would develop the curriculum, training programs, and evaluation tools to carry out the program. The program would adapt the monitoring system employed by the Ayrton Senna Institute in its programs to reduce age-grade distortion.

27. Next, the program would support a MOR program to keep the most vulnerable students in school, called *Bolsa Escola* (not to be confused with the federal *Bolsa Escola* program, which was folded into *Bolsa Familia* in 2003). *Bolsa Escola* supplements the federal *Bolsa Familia* program and improves learning for the poorest children by conditioning cash transfers to families on regular student school attendance, which is fundamental to performance. The MOR is seeking to complement this program with literacy programs for parents, which would further enhance the learning environment for the most vulnerable children of Recife.

28. Furthermore, the Project would support accelerated learning programs for the early years (1-5) of fundamental education. This includes, specifically, two programs implemented in partnership with the Ayrton Senna Institute: *Se Liga* and *Acelera Brasil*. Currently the two programs serve 2,419 students. They are both targeted to children who are at least two years above the target age for their grade level and are either functionally illiterate (in the case of the first program) or literate (in the case of the second). In 2010, 96 percent of students who entered *Se Liga* exited the program literate, according to test results from the implementing agency. Also in 2010, 98 percent of students in *Acelera Brasil* exited to re-enter their age-appropriate grade. The Project would monitor the performance of these students after concluding the program to see if they are able to continue to keep up with their age-appropriate grade; SEEL has a sufficiently advanced database to permit this.

29. ***Sub-Component 1(d): Professional Development of the Municipal Teaching Force***. The Project would support the professional development of the MOR's teaching force, including the provision of in-service training to teachers and directors at both the early child education

level and the fundamental education level. It would provide support to innovative efforts to provide in-service training to teachers and directors at both the early child education level and the fundamental education level. In particular, the MOR has implemented a new teacher training program in partnership with the Institute for Quality Teaching (*Instituto de Qualidade da Educação* -- IQE), which includes a combination of out-of-classroom training and teacher observation in order to help teachers implement effective teaching skills in the classroom. The jump from learning skills to their successful application is a missing link in many teacher evaluation programs.

30. ***Sub-Component 1(e): Education Management.*** The Project would provide support to education management, including: (i) the implementation of School Management Plans; and (ii) the expansion of information on student performance in the MOR's territory, through the reformulation and strengthening of the municipal system of student assessment (*Sistema Municipal de Avaliação da Rede* -- SMAR). First, empowering schools to implement their own programs of improvement and reform has been demonstrated in several countries to be effective (e.g., Nicaragua, Guatemala, El Salvador).[7] Along these lines, the MOR has initiated a program of School Management Plans; schools develop their own improvement plans but receive face-to-face support from headquarters for implementation of activities, improving administrative processes, and providing accountability for resources transferred from headquarters for implementation of the plan. The Project would support the implementation and monitoring of these plans.

31. An important ingredient to schools being able to strengthen performance is information, and the Project would support expansion of information on student performance in the MOR. Evaluation of student performance is essential to identifying weaknesses and providing struggling students and schools with the support they need. As such, the Project would support the reformulation and strengthening of the SMAR. This was initially implemented in 2007 as an initial evaluation, but the MOR now intends to implement it annually. The MOR currently participates in the national and state standardized examinations, but the municipal system would allow identification of weaknesses in student performance earlier in the education process and subsequent intervention in schools with poor performance. Whereas the national evaluation tests students in mathematics and Portuguese in the 3rd (optionally), 5th, and 9th years of fundamental education and 3rd year of upper secondary school, and the state evaluation tests students in those same years, the municipal test would evaluate the other years of fundamental education: 4, 6, 7, and 8. These data on student performance would permit constructive intervention early on. It would also uniquely permit tracking of value added for each year, permitting more consistent monitoring of teacher training and other educational interventions.

32. **Component 2: Strengthen institutions for more efficient and effective public management** ***(Estimated total cost: US$30.0 million; Bank: US$30.0 million)***. This component would provide technical assistance to strengthen the MOR's public management in the following areas: (a) educational evaluation and administration; (b) tax administration; (c) public debt management; (d) increasing efficiency of public expenditures; (e) municipal

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[7] Bruns, B, D Filmer, and HA Patrinos, "Making Schools Work: New Evidence on Accountability Reforms," World Bank: 2011, pp. 104-107.

planning, results-based management, and Project management; and (f) urban mobility management.[8]

33. ***Sub-Component 2(a): Education Evaluation and Administration (estimated cost US$1.45 million)***. Component 1 demonstrates the array of areas in which the MOR is innovating in order to improve both access to early child education and quality of primary and lower secondary education. As a SWAp, it includes programs for which the MOR already has budget items. Inclusion of education in Component 2 as well allows for the MOR to innovate in ways that are not already included in existing budget items, including evaluation, which is crucial in the context of the innovations that are taking place. This sub-component would provide support for: (i) the monitoring and evaluation of various key programs, including the accelerated learning programs, the expanded school day program, the School Management Plans program, and in-service education program; (ii) the carrying out of a study of the management of the education sector as a whole within the MOR's territory, identifying key strengths and weaknesses in the management system; (iii) the carrying out of a study of education expenditures; and (iv) the implementation of an improved monitoring system for the SEEL. With respect to the Project evaluations, the MOR has reason to expect successful results in each of the cases, but the details of design and implementation are critical. In-service training for teachers is a perfect example, where high-quality research has demonstrated in-service training to be highly effective in some cases and completely ineffective in others. Likewise, full-day schooling has been shown to be an effective intervention for improving quality, but only if the additional time is used effectively. For this reason, the evaluations would likely include in-class observation of teacher time use, using a system that has been implemented in the states of Pernambuco and Minas Gerais, as well as Rio de Janeiro municipality (the Stallings classroom observation method).

34. Beyond specific program evaluations, this component would support an improved monitoring system for educational data, incorporating student evaluation data, enrollments, attendance of students and teachers, and other key information for monitoring and planning. The analysis of expenditures within SEEL would support improved planning and management. In response to this analysis, this sub-component would support targeted training for education management at headquarters, study tours, and other areas as identified in the management study. The training for management would be guided specifically by the results of the management study.

35. ***Sub-Component 2(b): Tax Administration (estimated cost US$7.1 million)***. This sub-component would provide technical assistance for improving the administration of tax and non-tax revenues, including: (a) the planning and carrying out of a selective property registration exercise (*recadastramento*) in the urban areas to broaden the IPTU tax base; (b) the planning and carrying out of a property assessment exercise to update the outdated property values, which in turn serve as the base of calculation for IPTU and other MOR's taxes; (c) the carrying out of a communications campaign to facilitate planning and implementation of the property assessment

[8] Some activities under this component would complement a technical assistance loan by the Inter-American Development Bank (IDB) currently under execution (National Program to Support the Administrative and Fiscal Management of Brazilian Municipalities - PNAFM, which includes the MOR as one of the municipalities covered by the loan).

exercise referred to in (b) above, and the provision of assistance to ensure that the recommendations of the property assessment technical proposal are in line with the MOR's legal framework; (d) the development of a new tax management system, which includes a cadastre and a module for follow up of non-tax active debt; (e) the improvement of SEFIN e-services to facilitate voluntary tax compliance, as well as the carrying out of a campaign to expand automatic IPTU payment through bank accounts; (f) the development of a management system for the MOR's attorney general's office to manage legal claims resulting from the collection of tax debt and non-tax active debt; and (g) the purchase of IT equipment for the MOR's Secretariat of Legal Affairs (*Secretaria de Assuntos Jurídicos* -- SAJ).

36. ***Sub-Component 2(c): Public debt management (estimated cost US$0.29 million)***. This sub-component would provide technical assistance to enhance debt management, including: (a) carrying out an in-depth diagnostic of debt management to identify the system's main deficiencies and preparation of terms of reference (TOR) for the design of a new information system; (b) the development of a debt management system; (c) the design and completion of a training program for SEFIN staff working in debt management; and (d) the purchase of Information Technology (IT) equipment for SEFIN's debt management unit.

37. ***Sub-Component 2(d): Increasing efficiency of Public Expenditures (estimated cost US$8.5 million).*** This sub-component would support the MOR's efforts to enhance public sector efficiency in four main areas: (a) payroll management and human resources management; (b) procurement; (c) public financial management; and (d) modernization of the Municipal Information Technology Company (*Empresa Municipal de Informática* -- EMPREL). Activities would include: (a) the preparation of an in-depth diagnostic of human resources management in the MOR's territory, particularly focusing on improving payroll policy, the payroll system, and supporting the MOR in the design of a payroll audit; (b) the carrying out of a payroll audit and the acquisition of management tools to facilitate the execution of continuous controls once the audit mentioned herein is carried out; (c) the establishment of a new human resources management and payroll system, including modules for payroll, human resources management and pension management; (d) the provision of training for payroll management personnel; (e) the acquisition of IT equipment for the payroll management unit within the MOR's Secretariat of Public Administration and Personnel Management (*Secretaria de Administração e Gestão de Pessoas* -- SADGP) and the General Comptroller's Office (*Controladoria Geral do Município* – CGM); (f) the development of a procurement system to enhance contract management, including the provision of training and the acquisition of IT/office equipment for staff working at the procurement unit within SEFIN; and (g) the provision of support to comply with the federal government of the Federative Republic of Brazil's legislation on accounting standards, including the provision of training, and the acquisition of IT equipment for staff working at the accounting unit within SEFIN, including EMPREL.

38. ***Sub-Component 2(e): Municipal planning, results-based management, and Project management (estimated cost US$6.26 million)***. This sub-component would provide support to the MOR to: (a) create and implement a strategic priorities management unit within SEGESP, and develop indicators for these strategic priorities and link said indicators to the MOR's annual budget; (b) design and implement a training program in results-based management for managers and key staff in various MOR's secretariats, including SEGESP; (c) carry out of a reengineering

and simplification process of several management processes in key MOR's secretariats, and (d) Project management, including the hiring of key Project staff, the Independent Verification Agency (IVA) for the carrying out of technical audits, and Operating Costs.

39. ***Sub-component 2(f) Urban mobility management (estimated cost US$6.4 million)***. This sub-component would provide support to improve urban planning and management, including: (i) implementation of a traffic and transport integrated data center in Company of Urban Transport and Traffic *(Companhia de Trânsito e Transporte Urbano* -- CTTU), which would merge data from existing traffic and transport monitoring systems to improve more effective management of mobility within the MOR's territory; and (ii) preparation of Urban Plans to improve mobility in key areas of the MOR's territory, as well as design of specific investments within those Urban Plans.

B. Project Financing

Lending Instrument

40. The Specific Investment Loan of US$130 million to co-finance multi-sector interventions and activities would be disbursed between September 2012 and April 2018. The lending instrument was defined based on the Government's needs and to leverage the benefits of a Bank-financed operation to a broader scope. To this end, the Project would follow (a) a SWAp under Component 1, and (b) a traditional investment approach under Component 2.

41. The EEP are a sub-set of existing programs in the education sector, part of the MOR's current PPA (2010-13) and annual budget 2011, which have been selected as priority programs to be supported by this operation.[9] Such programs include investment and recurrent expenditures.[10] The next PPA cycle would cover years 2014-17 and should be submitted to the approval of the municipal Legislative body by August 2013. Since the Project is expected to conclude in 2017 (with closing date on April 30, 2018), the 2014-17 PPA is expected to keep the programs selected as EEP under this Project, which are detailed in Annex 3.

42. The Project would take a results-based financing approach to the implementation of agreed policies and programs. Thus, under Component 1, SEEL is expected to achieve specific results, which would then trigger disbursements. In addition, SEFIN, SADGP, and SEGESP would also be required to fulfill public management and implementation-related indicators to trigger disbursements under that component. The Project preparation team has selected a total of 12 Disbursement-linked Indicators (DLIs) that are challenging but realistic and that positively support achievement of the PDO.

[9] The four EEPs in the MOR budget are: 1206 – Effective Organization for Teaching and Learning; 1207 – Effective Support for Quality Education; 1214 – Social Assistance to the Municipal Students; and 2110 – Management of the Education Municipal Policies. Such programs include projects and activities as outlined in Annex 3.

[10] Percentage of expenditures by type in the education budget as a whole varies by budget line, but, in general, investment expenditures account for 6%, and recurrent expenditures for 94%, out of which payroll is about 53%.

Table 1: Disbursement Linked Indicators (DLIs)

DLI #	Indicators	Target by the end of the Project
1	Percentage of aggregate budget allocation for EEPs spent	At least 60%
2	Number of children enrolled in the Multi-Sectoral Early Child Development Program	1,200
3	Number of students enrolled in extended school day program	3,950
4	Percentage of all early child education facilities with emergency needs (first number) and priority needs (second number) that received required rehabilitation	100% of emergency and 80% of priority rehabilitation carried out each year
5	Number of students in Grades 1-5 enrolled in accelerated learning programs	900
6	Number of ECE professionals who have received in-service training	1,500
7	Percentage of teachers, directors, and pedagogical coordinators in fundamental education who received in-service training	82%
8	Number of schools that received systematic follow-up on School Management Plan from the Core Regional Follow-up team	120
9	System for learning assessment at the primary level	Implemented, at Level 4 of functionality (defined in Annex 1)
10	Quality of the MOR's tax administration system	Implementation of property reassessment
11	Efficiency of payroll management	New payroll system fully functional
12	Maintain key staff during the Project implementation period	Yes: Key staff defined in Annex 1

Project Cost and Financing

Table 2: Project Costs and Financing

Project Components	Project cost	IBRD Financing	% Financing
1. Expand coverage of improved ECE and create conditions conducive to learning in fundamental education	762,543,080	100,000,000	13%*
2. Strengthen institutions for more efficient and effective public management	30,000,000	30,000,000	100%
Total Baseline Costs	**792,543,080**		
Physical contingencies	92,160,000		
Price contingencies	36,571,920		
Total Project Costs	**921,275,000**	130,000,000	14%
Interest During Implementation			
Front-End Fees**	325,000		
Total Financing Required	**921,600,000*** **	**130,000,000**	14%

* % of financing in this table is based on the ratio of IBRD financing and Project cost for Component 1. Given SWAp characteristics, a percentage of financing up to 30 percent has been agreed upon for the EEP under Component 1 of the Project.

** According to the loan financial terms selected by the MOR, the FEF (325,000) would be paid from the MOR's own resources and not out of loan proceeds.

***Total Project costs were calculated based on the EEP's budget amounts for period 2011-17 plus Bank loan amount. Budget amounts per year were based on 2011 Annual Budget Law (LOA), proposed LOA 2012, and forecasts for 2013-2017 by introducing an inflation rate of 4.5 percent per year. Exchange rate US$1 = R$1.8536 (Dated September 30, 2011- Project Appraisal; source: Central Bank of Brazil).

C. Lessons Learned and Reflected in the Project Design

43. The proposed Project has been designed taking into account lessons learned from analytical work in Brazil and elsewhere as well as previous Bank operations in Brazil. The focus on expanding access to early child education stems from extensive work both in Brazil and internationally demonstrating high returns to early child education, both at the pre-school level and at the *creche* level. Analytical work specifically in the north-eastern region of Brazil supports the results on long-term returns to early child education. Furthermore, recent research in six state capitals across Brazil demonstrates the importance of quality in early child education. Children who attended low quality early child education centers performed similarly to children who attended no early education at all: Only high quality education centers had a positive impact on child development. For that reason, the Project would support the provision of materials and teacher training to ensure that children receive quality stimulation while at early child education centers. Recent evidence from Rio Grande do Sul in Brazil also demonstrates the developmental benefits of a multi-sectoral home-based early child development program, a pilot of which is supported by the Project.[11]

44. At the level of fundamental education, the emphasis on quality of learning is based on strong evidence that actual learning in school is a much better guarantor of both individual returns and economic growth in the long run than is simply school attendance.[12] Furthermore, extensive research (cited earlier) has demonstrated the importance of sufficient academic learning time and the effective use of that time for improving student performance, hence the interventions to expand the school day and to improve the quality of teaching within the school day through training. Accelerated learning programs like those supported by this Project have been included in several other Bank-supported projects – in the Acre Social and Economic Inclusion and Sustainable Development Project (P107146, Loan No. 7625-BR), the Pernambuco Education Results and Accountability SWAp (P106208, Loan No. 7711-BR), and the Rio de Janeiro State Fiscal Sustainability, Human Development, and Competitiveness Development Policy Loan Project (P117244, Loan No. 7827-BR) – and have been correlated with reductions in age-grade distortion. Finally, the State of Pernambuco has implemented several closely related programs to those of Recife – accelerated learning, lengthened school day, student evaluation – and so the Project would encourage close collaboration between the state and the MOR to harness those lessons. Some of these have been in the context of the above mentioned Pernambuco Education Results and Accountability SWAp.

45. In terms of public management, the recent successful modernization of property tax administration in municipalities such as Belo Horizonte in Brazil, as well as Cartagena and Barranquilla in Colombia, have informed the design of the tax administration sub-component 2(b) by including adequate planning and communication campaigns to accompany technical activities of property assessment and improvement in tax management systems, among other

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[11] All this evidence is documented in Evans D & K Kosec, "Early Child Education: Making Programs Work for Brazil's Most Important Generation", World Bank study, 2012.

[12] Hanushek E and L Woessman, "The Role of Cognitive Skills in Economic Development," Journal of Economic Literature, 46(3), 607-668, 2008.

activities.[13] The Bank's operational experience in payroll audits and upgrades in the cadastre of public servants in projects such as the Municipal Pension Reform Project (P074777, Loan No. 4673-BR) covering several municipalities, the Alagoas Fiscal and Public Management Reform Project (P103770, Loan No. 7817-BR) and the State Pension Reform II Technical Assistance Loan (P089793, Loan No. 7428-BR) has informed the design of this Project by, for example, dividing into separate activities the identification of anomalies and the implementation of the correcting measures, and would be further used in the design of the activities under sub-component 2(d). In addition, the Bank's extensive experience on results-based management in Brazil in several state and municipal-level projects, including Ceará Inclusive Growth SWAp (P106765, Loan No. 7600-BR), the Minas Gerais Partnership II SWAp (P101324, Loan No. 7547-BR), the above mentioned Pernambuco Education Results and Accountability SWAp, Rio Grande do Sul Fiscal Sustainability Development Policy Loan (P106767, Loan No. 7584-BR), and the Rio de Janeiro Municipality Fiscal Consolidation for Efficiency and Growth Development Policy Loan (P111665, Loan No. 7942-BR), would also be used in the Recife context to plan activities under sub-component 2(e).

46. Finally, the MOR is currently carrying out another Bank-supported project, *Capibaribe Melhor* (P089013, Loan No. 7497-BR), from which this Project has learned. That project has had great difficulty disbursing funds, and as a result this Project is taking several steps, including advance preparation of terms of reference and has a few large items (such as the payroll system) which would use a large portion of the technical assistance component during the first years of Project implementation.

IV. Implementation

A. Institutional and Implementation Arrangements

47. The Recife SWAp is a multi-sector Project, covering education and a wide range of public management activities. Given its nature, the Project would be implemented by five different municipal secretariats, but would also benefit several other secretariats and institutions. The five participating entities are SEGESP, SEEL, SEFIN, SADGP, and the Secretariat of Public Services (SSP). Project activities would also benefit SAJ, CGM, EMPREL, CTTU, and other mobility-related agencies. Thus, administration mechanisms require a certain degree of complexity but would count on a centralized coordinating body and a Project Operational Manual (*Manual Operacional do Projeto* -- MOP) detailing Project implementation arrangements.

48. SEGESP would be in charge of overall Project coordination and monitoring, and, as such, it would be the Bank's main interlocutor during Project implementation. It would be in charge of Project financial management issues. It would also be a participating entity responsible for carrying out sub-component 2(e). As the formal Project implementing agency, it would compile

[13] See Pinto Domingos, O., "Implementing Local Property Tax Reform in Brazil", *Land Lines,* Lincoln Institute of Land Policy, January 2011; World Bank, *Colombia: Rapid Action Plan for Improving Public Management in the Municipality of Cartagena de Indias,* 2009; and World Bank, *Colombia: Evaluation and Rapid Action Plan for Improving Public Management in the Municipality of Barranquilla*, 2010.

all Project-related information furnished by the other participating entities and produce the Project reports as required by World Bank policies and described in the Loan Agreement. It would also lead a Consultative Committee, and host a Project Implementation Unit (PIU) to be staffed with professionals, with TOR and qualifications acceptable to the Bank, in charge of providing cross support to all other participating entities. This Project would finance a deputy coordinator, a procurement specialist, a financial management specialist, and five consultants to act as focal points in the five participating entities. The MOR would also support, as part of the PIU, an overall Project coordinator, a financial coordinator, and two support staff. The key staff (at least the deputy coordinator, a procurement specialist, a financial management specialist, and at least three focal points) should be in place not later than two (2) months after Effectiveness date and would be kept throughout Project implementation.

49. SEEL would carry out Component 1, with responsibility for implementing all selected EEPs to be supported by the Project, and sub-component 2(a) through the carrying out of studies and assessments. SEEL would need support in drafting of TORs and even for the implementation of the EEPs. Analysis indicates the need to hire three to five professionals, specialized in education, management and monitoring and evaluation, to support SEEL.

50. SEFIN would carry out sub-components 2(b), (c), and part of (d). Some of these activities would also benefit SAJ, the CGM, and EMPREL. Because the municipal Bidding Committees are part of SEFIN's organization structure, it would be in charge of all procurement actions under the Project, relying on the procurement specialist situated in the PIU in SEGESP. Finally, SEFIN would provide data on the percentage of aggregate budget allocation for EEPs spent (DLI#1).

51. SADGP is in charge of personnel management including payroll, and would be responsible for the implementation of most activities under sub-component 2(d). Its roles and responsibilities for these activities would be similar to SEEL and SEFIN. Since this area requires substantial reforms, SADGP would dialogue with important stakeholders, particularly SEFIN and SEGESP, to ensure proper implementation and achievement of desired results.

52. Finally, the SSP would be in charge of sub-component 2(f), responsible for coordinating and conducting the urban mobility management-related activities and studies through the interaction with CTTU (which is not a participating entity) and any other relevant institutions. Like the other secretariats, it would provide to SEGESP the required technical and financial information for the purposes of Project implementation and monitoring.

B. Results Monitoring and Evaluation

53. SEGESP would have primary responsibility for tracking progress related to Project outcomes and results. SEGESP would provide inputs for sub-component 2(e) (Municipal planning, results-based management, and Project management) and would coordinate inputs gathered by SEEL for Component 1 (Expand coverage of improved ECE and create conditions conducive to learning in fundamental education) and sub-component 2(a) (Education evaluation and administration); SEFIN for sub-components 2(b) (Tax administration) and 2(c) (Public debt management); SEFIN and SADGP for sub-component 2(d) (Increasing efficiency of public

expenditures); and SSP for sub-component 2(f) (Urban mobility management). In the case of urban mobility management, information would also be prepared by the CTTU, the Greater Recife Consortium on Transport (*Consórcio Grande Recife*) and the Recife City Institute (*Instituto da Cidade do Recife Engenheiro Pelópidas Silveira*), and submitted to SSP for review and consolidation.

54. SEGESP would include the following information in each Project report: (a) the MOR's compliance with the DLIs; (b) the updated procurement plan; (c) a section describing any condition which interferes or that could potentially interfere with Project implementation, including any environmental/social issues that may arise during Project implementation. The Project reports would cover one semester and be submitted to the Bank twice a year prior to the respective disbursement requests, but not later than 60 days after the end of the period covered by such report.

55. The MOR would, not later than eighteen months months after Effectiveness date, select and contract an entity, independent from the MOR (Independent Verification Agency) with experience and qualifications in education acceptable to the Bank. The IVA would be responsible for the carrying out of at least two technical audits during the Project, particularly focused on the achievement of the DLIs, and submitting them to the Bank no later than the 6th and 11th withdrawal of funds under the Project.

C. Sustainability

56. Some of the education programs, such as those aimed to reduce age-grade distortion, are expected to run for several years and then, with the elimination (or significant attenuation) of the problem, be retired. Others, such as expansion of the school day, would be incorporated into the ongoing operational budget of the MOR.

57. Component 2 would support the MOR in addressing its fundamental municipal management problems, including tax administration and efficiency of public expenditures, with a special focus on payroll management. Due to the structural nature and political cost of some of these reforms, full implementation following completion of technical work is expected to represent the biggest challenge. Given the structural nature and urgency of these activities, these policies are likely to be sustained over time once implemented. The MOR's strong commitment to improvements in all the different public management sub-areas has been evidenced during the preparation of the Project and political authorities of the concerned secretariats have explicitly requested and endorsed the Project's activities. While a new administration may take office during Project implementation, the structural and urgent nature of the MOR's main public management challenges supported by this Project would very likely remain as top priorities. Studies in urban mobility management have the goal of making the CTTU a stronger coordination body, charged with periodically updating the Mobility Plan to increase accessibility, affordability, availability and acceptability of public transport in Recife.

V. Key Risks and Mitigation Measures

A. Risk Ratings Summary

Stakeholder Risk	Moderate
Implementing Agency Risk	
- Capacity	High
- Governance	High
Project Risk	
- Design	Substantial
- Social and Environmental	Moderate
- Program and Donor	Low
- Delivery Monitoring and Sustainability	Moderate
Overall Implementation Risk	High

B. Overall Risk Rating Explanation

58. The overall implementation risk is considered High, largely driven by the possible change in administration in early 2013 and MOR's limited previous experience with World Bank processes in procurement, and the consequent risks associated with capacity and governance. The capacity risks associated with a potential change in administration would be mitigated including through involvement of technical staff at each level of the MOR so that turnover after an election would not entirely eliminate capacity. The Project would have a detailed MOP, which would assist new counterparts in capacity building. Capacity risks associated with limited previous experience in Bank processes would be mitigated, including through training in procurement, as well as Project support for key staff who would specialize in this area. Governance risks stemming from potential political interference in institutional arrangements would be mitigated, including through hiring of a deputy coordinator for the Project with terms of reference and qualifications acceptable to the Bank, as well as creation of a Consultative Committee with structure and functions satisfactory to the Bank, as defined in the MOP.

VI. Appraisal Summary

A. Economic and Financial Analysis

59. Although estimating a rate of return for the Project overall is subject to enormous imprecision, the interventions related to this Project are expected to have significant returns. Early child education has been demonstrated to show significant impacts, the best example being a 7-10 percent rate of return on the United States-based Perry Pre-school Program. Estimates from northeastern and southeastern Brazil are between 12.5 percent and 15 percent. Rehabilitation to improve existing ECE centers is expected to yield improved physical and social development, per recent studies in Brazil, both of which are correlated with increases in earnings. The MOR is piloting – in this Project – a multi-sectoral early child development

program which is expected to include home-based cognitive stimulation, as a potential alternative to future expansion of public centers.

60. The projection of the fiscal situation of Recife over the period 2011-27 considers two scenarios (detailed in Annex 6). The baseline scenario, following the present trend of Recife's deteriorating economic position within the state, shows a difficult situation, even under the assumption of controlling expenditures on personnel and goods and services. The loss of economic position and therefore tax and transfers would reduce investment and jeopardize municipal infrastructure, throwing the MOR into a vicious circle.

61. The second scenario includes the World Bank loan of US$130.0 million, mainly expanding coverage of early child education and creating conditions more conducive to learning in fundamental education (US$100.0 million) but also improving municipal public management. Among the areas to be addressed, improvement in tax management, better control of current expenditures, and additional revenue should all permit the MOR to increase investments. Assignment of resources to payroll data systems would help to control personnel expenses as well as to evaluate risks related to the pension system. Modernization of debt control would reduce the risk of accumulating hidden liabilities that may jeopardize the fiscal situation.

62. Compared to the baseline scenario, the primary balance is improved under the second scenario despite the higher debt. In contrast to the baseline scenario, personnel expenses are stable around 46.3 percent, even in the face of expansion of services provision. The ratio of net debt to net current revenue (NCR) is higher than in the baseline scenario until 2018, given the Bank loan. For the same reason, the ratio of debt service to NCR equals the baseline scenario only in 2022. As previously stated both indicators are under acceptable limits.

B. Technical

63. This Project addresses a major constraint to growth in the MOR: the quality of learning. As discussed earlier, Recife lags behind the rest of the country both in coverage of children in early child education and in results of quality education. Evidence from around the world demonstrates that student learning is directly linked to both individual incomes upon the conclusion of school and to growth of the region as a whole. As such, Recife's poor performance is a clear obstacle to improved growth in the region and reduced poverty for individuals in MOR. As such, the investments in ECE (which have been shown to improve the quality of later learning) and the direct investments in fundamental education quality are greatly needed.

64. In terms of Component 2, the proposed activities are designed to address structural problems for the improvement of the MOR's public sector core management functions and to guarantee its contribution as a crucial element to improve Recife's socioeconomic conditions, enhancing the Government's capacity to promote economic development and social welfare from a cross-sectoral approach.

C. Financial Management

65. The Bank performed a Financial Management (FM) assessment in accordance with OP/BP 10.02 (Financial Management) and the Financial Management Practice Manual (issued by the Financial Management Sector Board in March 1, 2010) at SEGESP since it is the Project entity in charge of overall Project coordination and FM issues. The scope of the assessment included: (a) an evaluation of existing financial management systems to be used for program monitoring, accounting and reporting; (b) review of staffing requirements; (c) review of the flow of funds arrangements and disbursement methodology; (d) review of internal control mechanisms in place; (e) discussion in regard to reporting requirements, including the format and content of unaudited Interim Financial Reports (IFRs); and (f) review external audit arrangements.

66. The assessment identified as a major risk the lack of proper internal control arrangements. Thus, there is an inherent risk of insufficient appropriately skilled local-level resources and processes to adequately implement the Project. To mitigate these risks, the PIU to be created at SEGESP and properly staffed, including a financial management specialist supported by the Project and a financial coordinator supported by MOR, would be responsible for the various supporting FM tasks, to be detailed in the MOP, and for assuring a smooth flow of information and observance of Project arrangements within all participating entities, including SEFIN, which would be responsible for supplying the budget expenditure data that would be needed for disbursements. SEGESP's compliance with these requirements would be reviewed throughout the Project lifecycle.

67. The overall conclusion on the assessment of SEGESP is that the FM arrangements, as set out for the proposed Project, when operational, are considered adequate. Fiduciary Risks have been identified as Moderate (Annex 3, Table 1) and mitigated as reflected in the Operational Risk Assessment Framework (ORAF). The Project would support the hiring of a financial management specialist to assist with FM.

D. Procurement

68. SEFIN would be the Secretariat responsible for the procurement aspects of the Project. A procurement assessment of the capacity of SEFIN to implement procurement actions was carried out in March 2011 and updated in May and August 2011 by the Bank's procurement specialist for this Project. The assessment reviewed the organizational structure for implementing the Project and the interaction between the participating entities and SEFIN, in which the central unit for procurement processes is located. The team has a well functioning procurement staff who has experience in procuring goods and services, but no experience with the World Bank guidelines. There is no experience with processes to hire consulting services. The procurement specialist to be hired under the Project would strengthen the capacity of the MOR to implement the Project.

E. Social (including Safeguards)

Social Impacts and Risks

69. Overall the Project is expected to have a positive social impact, via the positive social impacts of quality early child education, multidisciplinary early child stimulation, and quality fundamental education. Significant long-term evidence from around the world demonstrates benefits of early child investments across a range of social outcomes. The focus on addressing the quality of education in Recife, which has fallen behind other major municipalities in Brazil, would help to provide more equitable access to a quality education.

70. The key stakeholders in the Project include parent associations, teachers, teachers' unions, Civil Society Organizations (CSOs) involved in education delivery, taxpayers, public servants, and the municipal administration. During Project preparation no traditional indigenous communities were identified in the municipal areas where the Project would be active. The MOR has several ongoing consultative forums for involving key stakeholders in issues of education policy design and implementation. This includes the Municipal Education Conference (*Conferência Municipal de Educação*, or COMUDE), which holds periodic consultations with teachers, parent associations, educational agencies and CSOs, and which met in August 2011 to discuss the plans to improve early childhood education.

71. In addition to COMUDE, additional consultations have been held with CSOs involved in the education sector, representatives of teachers' unions, and community members in selected areas. These consultations highlighted: (a) the high level of demand for the CMEIs among both teachers and community members; (b) the importance of a holistic approach to improving early childhood education via equal focus on the quality of teaching (pedagogic content, teacher training); (c) the utility of linking *Bolsa Família* to access to CMEIs and to community activities held at the CMEIs; and (d) an interest among teachers in being involved in monitoring implementation of this Project, together with professionals from health and social protection.

F. Environment (including Safeguards)

72. ***Environmental Assessment (OP/BP 4.01)***. Project interventions imply some degree of rehabilitation activities, thereby triggering OP/BP 4.01 (Environmental Assessment). Most Project activities are not expected to generate adverse environmental effects. The Project involves selected rehabilitation of existing early child education centers on existing footprints. The appropriate Environmental Assessment tool is an Environmental Management Framework (EMF), which was prepared and disclosed on September 23, 2011 at www.recife.pe.gov.br and the World Bank's website. The EMF may be updated from time to time with the prior written agreement from the Bank. The EMF provides a description of the following: (a) the environmental mitigation and monitoring measures to be taken during implementation; (b) waste disposal measures; and (c) institutional arrangements for supervision and oversight of environmental measures. Safety measures would also ensure that students and teachers attending the schools where any construction activities are taking place are not negatively affected. As appropriate, each rehabilitation contract would specify the required environmental management measures to be followed at each site. Only rehabilitation that is on the existing building footprint would be eligible under the Project, and the Project therefore would not involve involuntary resettlement, social or economic displacement of persons or land acquisition.

Annex 1: Results Framework and Monitoring

FEDERATIVE REPUBLIC OF BRAZIL: Recife Education and Public Management Project

The objective of the Project is to expand coverage of improved early child education (ECE), create conditions more conducive to learning in fundamental education, and improve municipal public management, all within the MOR's territory

PDO Level Results Indicators	Core	Unit of Measure	Base-line	Cumulative Target Values [* indicates non-cumulative]					Frequency	Data Source/ Methodology	Responsibility for Data Collection	Description (indicator definition etc.)
				YR 1	YR 2	YR3	YR 4	YR5				
Indicator One: **Expand Coverage of Improved ECE**. Number of children enrolled in the Multi-Sectoral Early Child Development Program [DLI 2]	☐	Number	0	0	400	800	1,200	1,200	Annual	Enrollment records & contract with assisting agency	SEEL	Number of students enrolled in program with (1) policies integrated across sectors, and (2) individualized attention either at home or in existing buildings in the administrative region. SEEL would provide contract with agency assisting in design and implementation. Subject to IVA verification.
Indicator Two: Create Conditions More Conducive to Learning in Fundamental Education. Proportion of students successfully exiting accelerated learning programs*	☐	Percentage	90% (Jan 2012)	90%	90%	90%	95%	95%	Annual	Enrollment and test records	SEEL	% students passing pre-defined tests provided by implementing agencies in *Se Liga* and *Acelera Brasil*. Goal refers to

PDO Level Results Indicators	Core	Unit of Measure	Base-line	Cumulative Target Values [* indicates non-cumulative]					Frequency	Data Source/ Methodology	Responsibility for Data Collection	Description (indicator definition etc.)
				YR 1	YR 2	YR3	YR 4	YR5				
												average successful passing rate across all students in these two programs.
Indicator Three: Number of students enrolled in extended school day program* [DLI 3]	☐	Number	1,514 (Jan 2012)	2,450	3,450	3,950	3,950	3,950	Annual	Enrollment records	SEEL	Regular school day hours plus additional hours of instruction in math and Portuguese for students in bottom 40% of state evaluation. Includes students in Grades 3, 5, and 6-9.
Indicator Four: IPTU revenues increase in real terms	☐	Percentage	IPTU revenues of R$ 185.2 million (2010)	0%	0%	+12%	+25%	+30%	Annual – at the end of every fiscal year	Official IPTU annual collection data	SEFIN	Increase in real terms of IPTU revenues deducting the inflation rate according to the IPCA (Official Consumer Prices Index Enlarged).

PDO Level Results Indicators	Core	Unit of Measure	Base-line	Cumulative Target Values [* indicates non-cumulative] YR 1	YR 2	YR3	YR 4	YR5	Frequency	Data Source/ Methodology	Responsibility for Data Collection	Description (indicator definition etc.)
Indicator Five: Improved municipal management through a more efficient administration and stronger control on payroll, leading to savings on personnel expenditures	☐	Text	2011 central adm. payroll (Jan 2012)	Firm for payroll audit contracted	Audit completed and incorrect payments identified, equivalent to 3% of payroll	Implementation of payroll audit findings initiated	Reduced payroll compared to previous year of at least R$ 7.2 million, following implementation of audit findings	Controls over payroll management are effective for all central admin., validated by *Controladoria*	Annual – at the end of every fiscal year	Copies and reports of monthly payroll data (SEFIN) and documentation of identification and implementation of savings (SAGDP)	SEFIN and SADGP	Reduced payroll in Yr 4 would be generated by the identification and correction of mistakes in the payroll, calculated using the same staff contingent taken into account in the payroll audit planned by 2013, excluding retired staff and other staff excluded from the payroll for legal reasons.

Intermediate Indicators	Core	Unit of Measure	Base-line	Cumulative Target Values [* indicates non-cumulative] YR 1	YR 2	YR 3	YR 4	YR 5	Frequency	Data Source / Methodology	Responsibility for Data Collection	Description (indicator definition, etc.)
Intermediate Results Indicator 1: Percentage of aggregate budget allocation for EEPs spent [DLI 1]	☐	Percentage (minimum)	74.9 (2010)	60	60	60	60	60	Annual	MOR records	SEGESP	Baseline includes investment and recurrent expenditures, excluding payroll expenditures.
Component One: Expand coverage of early child education and create conditions conducive to learning in fundamental education												
Intermediate Result Indicator 2: Total number of Project beneficiaries and percent that are female*	X	Number (Percentage)	0	86,500 (48)	86,500 (48)	86,500 (48)	86,500 (48)	86,500 (48)	Annual	Enrollment records (*Sistema de Matricula do Municipio do Recife*)	SEEL	All ECE and fundamental education, students are included.

Intermediate Indicators	Core	Unit of Measure	Base-line	Cumulative Target Values [* indicates non-cumulative]					Frequency	Data Source / Methodology	Responsibility for Data Collection	Description (indicator definition, etc.)
				YR 1	YR 2	YR 3	YR 4	YR 5				
Intermediate Result Indicator 3: Percentage of all early child education facilities with emergency needs (first number) and priority needs (second number) that received required rehabilitation [DLI 4]	☐	Percentage	100% 85%	100% 80%	100% 80%	100% 80%	100% 80%	100% 80%	Annual	List of schools needs. Rehabilitation protocol signed by the facility director, the SEEL engineers, and the firm contracted to provide rehabilitation	SEEL	Emergency & priority needs are defined in Annex 2. SEEL will provide the list of schools requiring emergency and priority rehabilitation at the beginning of each year. At the end of each year, SEEL will provide the signed rehabilitation protocol verifying emergency and priority needs have been satisfied. Subject to IVA verification.
Intermediate Result Indicator 4: Number of CMEIs that received the complete package of materials ("enxoval completo") according to infrastructure needs	☐	Number	8	10	13	19	26	33	Annual	Check list of items received signed by the CMEI director	SEEL	The complete package of materials refers to all items on the "*Padrões de Qualidades para Unidades de Educação Infantil – Centros de Educação Infantil-CMEI / Creches*".

Intermediate Indicators	Core	Unit of Measure	Base-line	Cumulative Target Values [* indicates non-cumulative]					Frequency	Data Source / Methodology	Responsibility for Data Collection	Description (indicator definition, etc.)
				YR 1	YR 2	YR 3	YR 4	YR 5				
Intermediate Result Indicator 5: Number of students in Grades 1-5 enrolled in accelerated learning programs* [DLI 5]	☐	Number	2,419 (2012)	1,900	1,450	1,300	1,200	900	Annual	Enrollment records	SEEL	Accelerated learning programs refers to *Se Liga* and *Acelera Brasil.* Subject to IVA verification.
Intermediate Results Indicator 6: Number of ECE professionals who have received in-service training* [DLI 6]	☐	Number	1,000	1,050	1,150	1,250	1,350	1,500	Annual	Training records that include the name of professionals that satisfied the requirement and the courses completed.	SEEL	To be counted as having received in-service training, participants must satisfy at least 20 hours of training during the year. Subject to IVA verification.
Intermediate Results Indicator 7: Percentage of teachers, directors, and pedagogical coordinators in Fundamental Education who received in-service training* [DLI 7]	☐	Percentage	75%	75%	78%	80%	82%	82%	Annual	Training records that include the name of professionals that satisfied the requirement and the courses completed.	SEEL	Participants must satisfy at least 20 hours of training during the year. Percentage calculated by simple sum of total trained across teachers, directors, and coordinators, divided by total staff in those three groups. Subject to IVA verification.
Intermediate Result Indicator 8: Number of schools that received systematic follow-up on a school management plan from the Core Regional Follow-up team [DLI 8]	☐	Number	**35**	70	85	100	115	120	Annual	Reports from Core Regional Follow-up Team and school	SEEL	Standardized monitoring reports must be acceptable to the Bank, demonstrating

Intermediate Indicators	Core	Unit of Measure	Base-line	Cumulative Target Values [* indicates non-cumulative]					Frequency	Data Source / Methodology	Responsibility for Data Collection	Description (indicator definition, etc.)
				YR 1	YR 2	YR 3	YR 4	YR 5				
										management plans		detailed diagnosis of school challenges. Subject to IVA verification.
Intermediate Results Indicator 9: System for learning assessment at the primary level [DLI 9]	X	Text	0	1	2	3	4	4	Annual	Testing records & reports	SEEL	The system in the Municipality of Recife is called SMAR. Score equals 1 for implementation, with one additional point for each criteria listed below the indicator that is satisfied.
Data analyzed and results reported			No	No	Yes	Yes	Yes	Yes				
Data reported by gender, urban/rural, or geographic locations			No	No	No	Yes	Yes	Yes				
Assessments repeated at least once every 5 years for the same subject areas and grades			No	No	No	No	Yes	Yes				
Component Two: Strengthen institutions for more efficient and effective public management												
Intermediate Result indicator 10: Impact evaluation of main education programs	☐	Text	No impact eval-uation			Age-grade distor-tion correction program (second half of Funda-mental Education) IE	In-service teacher training IE	Extended school day IE	Annual	Completed impact evaluation reports	SEEL	Monitors the completion of 3 Impact Evaluations.

Intermediate Indicators	Core	Unit of Measure	Base-line	Cumulative Target Values [* indicates non-cumulative]					Frequency	Data Source / Methodology	Responsibility for Data Collection	Description (indicator definition, etc.)
				YR 1	YR 2	YR 3	YR 4	YR 5				
Intermediate Result Indicator 11: Quality of the Municipality of Recife's tax administration system [DLI 10]	☐	Text	No prop-erty reasse ssment carried out	TORs for firm to carry out property reassessment approved by Bank	New web-based system for IPTU collectio n fully function-al	Comple-tion of the property reassess-ment	Impleme ntation of property reassess-ment		Annual	IPTU collection system	SEFIN	"Property reassessment" means the establishment of new property values for the IPTU. "Completion" means to finish the technical reassessment. "Implementa-tion" means to apply the new property values to the IPTU.
Intermediate Result Indicator 12: Efficiency of payroll management [DLI 11]	☐	Text	Pay-roll system needs impro ve-ment	TORs for payroll audit and new payroll system approved by Bank	Completi on of payroll audit and identifica tion of potential savings	Correct-ive measures to address payroll audit findings are imple-mented, genera-ting annual savings to the munici-pality of at least R$ 7.2 million	New payroll system fully function-al		Annual	Progress report including documentatio n of achieved targets	SEFIN and SADGP	Completed payroll audit evidenced by approved completion of consultancy to realize audit. Implementation of new system evidenced by screen shots of new system.

Intermediate Indicators	Core	Unit of Measure	Base-line	Cumulative Target Values [* indicates non-cumulative]					Frequency	Data Source / Methodology	Responsibility for Data Collection	Description (indicator definition, etc.)
				YR 1	YR 2	YR 3	YR 4	YR 5				
Intermediate Result Indicator 13: Municipal planning and results-based management	☐	Text	Unit for Monitoring Strategic Projects is not fully functional	Completion of terms of reference for automation of key selected processes	Completion of mapping and automation of first 10 processes	Completion of results-based management training of 200 people	Com-pletion of auto-mation of all 30 pro-cesses	Unit for Monitor-ing Strategic Projects is fully functional with leadership by permanent civil servants	Annual	Progress report including documentation of achieved targets	SEGESP	Key selected processes are identified in Annex 2. Areas for 30 processes are in Annex 2; specific processes would be defined during Project implementation.
Intermediate Result indicator 14: Implementation of a traffic and transport integration data center	☐	Text	No integrated data center.	Technical mission to integrated traffic and transport data centers Preparation of a TOR by technical staff for a company to implement the data center Preparation of a TOR for company to train staff to operate data center	Hire firm to supply equip-ment and systems Acqui-sition of equip-ment Comp-lete data center pur-chased and installed Hire firm to train staff to operate the data center	Execu-tion and comple-tion of the training staff to operate the data center Comp-lete data center in opera-tion			Annual	Progress report including documentation of achieved targets	SSP with inputs from CTTU, Recife Consortium on Transport, and Recife City Institute	Data center in operation demonstrated by ability to generate reports based on transport data from various sources.

Intermediate Indicators	Core	Unit of Measure	Base-line	Cumulative Target Values [* indicates non-cumulative]					Frequency	Data Source / Methodology	Responsibility for Data Collection	Description (indicator definition, etc.)
				YR 1	YR 2	YR 3	YR 4	YR 5				
Intermediate Result indicator 15: Develop urban plans and priority projects to facilitate and expand the mobility of students in Recife's key metropolitan centers	☐	Text	Priority projects not yet prepared	Hire consultants to prepare a TOR for company to develop two urban plans	Hire consult-ing company to develop two urban plans Prepara-tion by contrac-tor of the urban plan of Boa Viagem & of City Center	Discus-sion of the two urban plans Contract-ing a firm to develop the priority projects	Preparation of the priority projects	Conclusion of the priority projects	Annual	Progress report including documentation of achieved targets	SSP	Urban plans lay out array of desired actions to improve mobility in a particular area. Priority projects are specific actions within those plans.

Intermediate Indicators	Core	Unit of Measure	Base-line	Cumulative Target Values [* indicates non-cumulative]					Frequency	Data Source / Methodology	Responsibility for Data Collection	Description (indicator definition, etc.)
				YR 1	YR 2	YR 3	YR 4	YR 5				
Intermediate Result indicator 16: Maintain key staff during the Project implementation period. [DLI 12]	☐	Yes/No	No	Yes	Yes	Yes	Yes	Yes	Biennial	Staff records	SEGESP	Key staff are defined as at least deputy coordinator, procurement specialist, financial management specialist, and three focal points in different Participating Entities. Personnel have experience and functions acceptable by the Bank and have been hired, and are working in the Project.

Annex 2: Detailed Project Description

1. **Component 1: Expand coverage of improved ECE and create conditions conducive to learning in fundamental education *(Estimated total cost: US$891.6 million; Bank: US$100.0 million)***. This component would provide support for the implementation of the EEPs in the following areas: (a) rehabilitate ECE centers; (b) promote multi-sectoral early child development; (c) create conditions more conducive to learning in fundamental education; (d) professional development of the municipal teaching force; and (e) education management.

2. ***Sub-Component 1(a): Rehabilitate ECE centers***. This sub-component would support minor rehabilitation of existing creches, preschools, and CMEIs. For rehabilitation, the MOR's education team and team of engineers defined emergency needs and priority needs, and agreed to address 100 percent of emergency needs identified in the beginning-of-year rehabilitation meeting and 80 percent of priority needs.

Emergency needs are defined as follows:

- Roof: Roofing displays risk of caving in (compromised wood, grave problems in sealing)
- Electricity: Open access to electric current
- Structure: Serious damage compromising people's physical safety
- Water and sanitation: Sewage leakage into classrooms or other educational spaces, or cisterns with problems compromising the quality of water in reserve

Priority actions are defined as follows:

- Roof: Re-covering the roof to fix leaks and compromises to the electrical system
- Electricity: Ensuring balance in the network to avoid burning equipment and lighting
- Structure: Waterproofing and fixing holes
- Water and sanitation: Repairs in the sewage system, expansions in capacity for water (construction of cisterns or other reserve locations)

3. ***Sub-Component 1(b): Promote multi-sectoral early child development***. This sub-component would support a new, multi-sectoral early child development program to reach children age 0-5. This program has a series of steps already defined: (a) develop a program of multi-sectoral action focused on holistic development of children age 0-5 years; (b) define and implement an ongoing training plan regarding early child development for management, technical, and teaching staff; (c) strengthen family competencies with a view to holistic development of children in the following areas: physical, cognitive, play, social interactions, and emotional development ("affect"); and (d) offer systematic subsidies for multi-sectoral early child development services as defined within the program.

4. ***Sub-Component 1(c): Create conditions more conducive to learning in fundamental education***. This would be achieved through provision of support to create conditions more conducive to learning in fundamental education, including: (i) extension of the school day with two additional hours of focused education in mathematics and Portuguese; (ii) support of a program to improve attendance for vulnerable students (School Grant, or *Bolsa Escola*), and (iii) support of two early-grade accelerated learning programs, Get Focused and Accelerate Brazil (*Se Liga* and *Acelera Brasil*).

5. This sub-component would support the expansion of the school day for students in the third grade, fifth grade, and sixth through ninth grades of fundamental education with a focus on Portuguese and mathematics. The expansion would be two hours per day, four days of the school week. This would require contracting of 110 new teachers in the third and fifth grades, and 66 new teachers in sixth through ninth grade, who would each teach two classes of the extended school day per day during four days of the week, with the fifth day reserved for training and preparation. The development of this program requires the following steps: (a) creation of pedagogical technical team, including eight professionals, who would coordinate and supervise the program, (b) contract external trainers to carry out the training of teachers, supervisors, and the monitoring team for the Project, (c) contracting of 35 supervisors, (d) contracting of 176 new teachers, (e) contracting of a learning monitoring system for the program, and (f) identification of which schools and students would take part in the program each year in the course of program roll-out.

6. This sub-component would also support *Bolsa Escola*, which provides support to poor children to keep them attending school (and thus enhance their learning capacity). Furthermore, this improves the quality of learning for less vulnerable children, as more vulnerable children improve their learning and are less likely to distract teacher attention with widely heterogeneous learning levels across the classroom. The *Bolsa Escola* program currently reaches just over 14,000 children.

7. Finally, this sub-component would support accelerated learning in the early grades of fundamental education. Early year (grades 1-5) accelerated learning programs for children who are literate and for those who are not literate are already in place in the MOR. *Se Liga* and *Acelera Brasil* target children who are at least two years too old for their grade level and are either functionally illiterate (in the case of the first program) or literate (in the case of the second). These programs are currently active all over Brazil. *Se Liga* is active in eight state systems and 802 municipal systems around the country *Acelera Brasil* is active in eight state systems and 727 municipal systems. Both programs have demonstrated positive results in other contexts, including reduce drop-out rates, higher grade promotion, and improved literacy.

8. ***Sub-Component 1(d): Professional Development of the Municipal Teaching Force.*** The MOR has a series of in-service training programs that would be supported by the Project. First, the Project would support early child education in-service training for managers, teachers, and daycare assistants (ADIs). Second, at the level of primary education (years 1-5), the Project would support a range of in-service training programs, including a program to train teachers to incorporate mathematics games in their various activities, a training program for teachers who have recently entered the school system, a training focused on literacy and basic writing skills, and a major training in Portuguese and mathematics education for most teachers across the system. The program would support a novel program of teacher training supported by IQE which incorporates some of the most promising elements of teacher training programs, including in-class observation of teachers by trainers, followed by feedback both individually and in groups. Elements of this training, currently implemented in just eight schools, are being adapted to a broader training program for the system which would be evaluated within the context of the Project. As in-service training programs tend to vary widely in quality, the Project would

evaluate the impact of the various programs on teacher time use and quality of student outcomes in the classroom.

9. ***Sub-Component 1(e): Education Management***. Finally, this sub-component would support ongoing management reform programs, including implementation support for school development projects, a municipal-level student evaluation (SMAR), and improved information systems for processing both the SMAR and data on profiles of students and teachers.

10. **Component 2: Strengthen institutions for more efficient and effective public management** ***(Estimated total cost: US$30.0 million; Bank: US$30.0 million)***. This component would provide technical assistance to strengthen the MOR's public management in the following areas: (a) educational evaluation and administration; (b) tax administration; (c) public debt management; (d) public expenditures, including payroll management and human resources management; procurement; public financial management; and modernization of EMPREL; (e) municipal planning, results-based management, and Project management; and (f) urban mobility management.

11. ***Sub-Component 2(a): Education Evaluation and Administration (estimated cost US$1.45 million)***. This sub-component would provide support for: (i) the monitoring and evaluation of various key programs, including the accelerated learning programs, the expanded school day program, the school improvement plans program, and in-service education program; (ii) the carrying out of a study of the management of the education sector as a whole within the MOR's territory, identifying key strengths and weaknesses in the management system; (iii) the carrying out of a study of education expenditures; and (iv) the implementation of an improved monitoring system for the SEEL. For part (i), it would include evaluation of some of the education interventions within the Project. Obviously, the resources are not sufficient to carry out a whole series of rigorous evaluations, so a range of methods would be employed, some more associated with careful monitoring over time and in other cases, more rigorous identification of impacts. First, the program would include evaluation of the program of accelerated learning to correct age-grade distortion. These programs have been implemented throughout Brazil but with very limited rigorous evidence to support them. In the implementation of early-grade accelerated learning, the Project would support a consultant to design an evaluation, ideally taking advantage of randomized assignment of the first year of roll-out among the universe of children in need of correction, measuring student performance at the end of the program in order to demonstrate whether students in accelerated learning programs in fact learn more than similar students in regular schooling. The precise identification strategy would be developed as the intervention is prepared. Second, the program would include evaluation of in-service training for teachers. This is likely to include in-class observation of teachers in order to record whether teachers who have undergone certain in-service training programs have improved their classroom time use relative to those who have not, seeking credible matching methods in general. With one teacher training intervention, that developed by IQE, which includes teacher observation and subsequent feedback both individually and in groups, the program is being adapted gradually and so the Project would encourage rigorous evaluation. Third, the program would include evaluation of the extension of learning time in school. In the State of Pernambuco, it has already been demonstrated that those schools with the extended school day attain the best results in the state-level evaluations. Similar evaluations would be carried out in Recife to ensure that the extended

day is being used effectively. This would likely be a difference-in-difference evaluation using administrative data. Finally, a similarly designed evaluation would be carried out to compare schools receiving significant support in the implementation of their school management plans, as opposed to schools not receiving such intensive support. All schools in Recife have a school management plan, and so the intervention of interest is not the existence of the plan but rather the intensive support in implementation provided from headquarters, creating an interesting hybrid of decentralized identification of needs with expert support from the center.

12. For part (ii), beyond the evaluation of specific interventions, a consultancy would be contracted to carry out a management analysis of the SEEL, with the objective of identifying strengths and weaknesses in effectiveness. For part (iii), a consultancy would realize a study of education expenditures to identify weaknesses and strengths in the use of education resources. Finally, the Project would support (iv) an improved monitoring system for the SEEL to ensure that the MOR has consistent, up-to-date information on students, teachers, their placement, etc., to improve planning. An example could be the Ayrton Senna system used in accelerated learning courses, but adapted to regular school classes in the MOR.

13. Based on the results of that study, the Project would fund some of the following activities: (a) training of the management team at the education secretariat, (b) study tours to other areas with highly effective education management or programs or the invitation of representatives of such programs to Recife, and (d) participation in conferences aimed to enhance knowledge of effective educational management and quality.

14. ***Sub-Component 2(b): Tax Administration (estimated cost US$7.1 million)***. This sub-component would provide technical assistance for improving the administration of tax and non-tax revenues, including: (a) the planning and carrying out of a selective property registration exercise (*recadastramento*) in the urban areas to broaden the IPTU tax base; (b) the planning and carrying out of a property assessment exercise to update the outdated property values, which in turn serve as the base of calculation for IPTU and other MOR's taxes; (c) the carrying out of a communications campaign to facilitate planning and implementation of the property assessment exercise referred to in (b) above, and the provision of assistance to ensure that the recommendations of the property assessment technical proposal are in line with the MOR's legal framework; (d) the development of a new tax management system, which includes a cadastre and a module for follow up of non-tax active debt; (e) the improvement of SEFIN e-services to facilitate voluntary tax compliance, as well as the carrying out of a campaign to expand automatic IPTU payment through bank accounts; (f) the development of a management system for the MOR's attorney general's office to manage legal claims resulting from the collection of tax debt and non-tax active debt; and (g) the purchase of IT equipment for the MOR's Secretariat of Legal Affairs.

15. The seven activities listed above fall into the following broader groupings:

(a) *Selective Update of IPTU's property inventory and re-assessment of property values for IPTU (estimated cost US$1,340,000).* This activity includes five consultancies: (i) review and update of properties in the areas with stronger urban growth in the last years through purchasing of air photos; (ii) planning and completion of a selective property registration exercise (*recadastramento*) in the newest urban areas; (iii) planning and completion of a property assessment exercise to update property values; (iv) a communications and institutionalization strategy for the planning and successful implementation of the reform; and (v) technical assistance to ensure legal viability of the property assessment technical proposal, considering recent experiences from other Brazilian municipalities such as Belo Horizonte and São Paulo.

(b) *Technical assistance for developing a new revenue administration system, replacing the current system Tributos Municipais (estimated cost US$4,050,000).* A first technical assistance consultancy would prepare the terms of reference and bidding documents for the procurement process for the development of the new system. The new system would include a cadastre of active and inactive debt for tax and non-tax revenues (fines, fees, penalties, licenses, etc.). This second activity would also include the training of the staff working on this system.

(c) *Technical assistance to improve voluntary tax compliance through the improvement of SEFIN's web-based tax collection system and the design of a communications campaign (estimated cost US$820,000).* This activity aims at facilitating tax, fees and other payments using bank accounts (*sistema débito em conta*) through the development of an improved web-based system, and a consultancy for designing a communications campaign to disseminate the advantages of this payment option.

(d) Strengthening of SAJ for enhancing tax debt management (estimated cost US$800,000). This activity would support the purchasing and adaptation of a management tool to improve portfolio management, the digitalization of legal opinions (pareceres) and an information management system to administer them, and the modernization of the Secretariat through the acquisition of equipments.

(e) *Technical assistance for drafting the terms of reference of the tax administration activities (US$90,000).* This TA would allow coordinating technically the terms of reference of the different activities included in this sub-component.

16. ***Sub-Component 2(c): Public debt management (estimated cost: US$0.29 million).*** Activities to be financed under the sub-component are as follows:

(a) *Preparation of a comprehensive diagnostic report on Recife's debt management (estimated cost US$75,000*), in order to identify the key areas for improvement. The consultancy would also prepare the terms of reference for the development of a new debt management system.

(b and c) Development of a new debt management system, including the training program for the staff working in this area and acquisition of equipment for the Debt Management Unit (estimated cost US$180,000). The system would allow the MOR to produce reports in real time, monitor debt payments and maturity more effectively. The report would be linked to Recife's financial management system.

(d) *Purchase of IT equipment for SEFIN's Debt Management Unit (estimated cost US$35,000).* This equipment will allow the implementation of this Unit's products (e.g., monitoring of debt payments and maturity, reports).

17. ***Sub-Component 2(d): Increasing Efficiency of Public expenditures (estimated cost US$8.5 million).*** This sub-component would include activities for the following sub-areas: (a) payroll management and human resources management; (b) procurement; (c) public financial management; and (d) modernization of EMPREL. Specific activities to be financed under this sub-component are as follows:

18. Payroll management and human resources management (estimated cost US$6,900,000)

(a) *Preparation of a comprehensive diagnostic report on Recife's human resources management and payroll management (estimated cost US$100,000).* The consultancy would focus mainly on payroll management, pay policy and human resources management objectives such as attraction and retention of qualified personnel. In addition to the diagnostic report, which would identify the main issues and prepare an action plan with sequencing of the technical reforms needed, this consultancy would support the MOR in preparation of terms of reference and bidding documents for the payroll audit (see next activity) and the terms of reference and bidding documents for the new HRM and payroll system (see below).

(b) *Payroll Audit of Recife's Central Administration (estimated cost US$1,180,000).* The audit is expected to be carried out by a private firm with experience in similar exercises in other Brazilian cities or states. The audit would focus on identifying weaknesses in internal controls during the payroll process across the Administration and would carry out a transactions audit to identify incorrect payments both for active personnel and retirees. The audit report would include an action plan to enhance internal controls for payroll management, and would identify efficiency savings to be achieved through the correction of payments. The MOR is expected to follow up on the implementation of the audit's findings by taking the necessary legal measures to improve controls and actually achieve these efficiencies though the discontinuation of incorrect payments.

(c) *Purchase of a new payroll and human resources management system (estimated cost US$4,700,000)* with technology transfer and permanent assistance, including modules for (i) payroll management; (ii) human resources management; and (iii) social security, addressed to the staff included in the *Regime Jurídico Único* and the *Regime Geral de Previdência Social.*

(d) *Strengthening of payroll management (estimated cost US$300,000*) by the design and implementation of a training program for staff working on payroll management across the SADGP and acquisition of equipment for the SADGP.

(e) *Strengthening the CGM's capacity to enhance control over the MOR's payroll (estimated cost US$620,000).* This activity would support the purchase and adaptation of a system for crossing databases with the objective of identifying incorrect payments to employees and retirees. This system would be operated regularly and would supplement the payroll audit, which represents a one-time effort. The activity would also include acquisition of equipment for the CGM.

19. Procurement (estimated cost US$400,000)

(f) *Modernization of procurement management* through the development of a system for management of contracts and bidding processes, implementation of a continuous training program for procurement staff and acquisition of equipment for the unit.

20. Public Financial Management (estimated cost US$300,000) and Modernization of EMPREL (estimated cost US$900,000)

(g) *Modernization of a system for data-collection to develop cost-accounting indicators.* Strengthening of financial and accounting management to comply with policy changes mandated at the national level, continuous training for staff, and acquisition of equipment for the unit within SEFIN. This would also include provision of new information technology systems and equipment for EMPREL.

21. ***Sub-Component 2(e): Municipal planning and results-based management, and Project management (estimated cost US$6.26 million)***. Activities planned under this sub-component are as follows:

(a) *Technical assistance to support the set up and implementation of a Unit for Monitoring of Strategic Projects, including the development of a system of strategic indicators (estimated cost US$1,400,000).* A consulting firm with experience in similar tasks in other Brazilian sub-national governments would provide capacity support to SEGESP for monitoring performance information of strategic projects in education and other key service-delivery sectors. The unit would provide performance information and would monitor financial and physical targets of strategic projects, providing decision-makers with timely information which would inform budget formulation and execution.

(b) *Technical assistance to design and implement a training program in performance management for 200 managers and key staff (estimated cost US$210,000),* particularly for the SEGESP team, in order to coordinate the MOR's efforts addressed to a gradual implementation of a performance management system.

(c) *Technical assistance to map and automate 30 key administrative procedures (estimated cost US$1,950,000).* Key processes to be mapped and automated are expected to be from the SEFIN, SEGESP, SADGP, SEEL, SAJ the CGM, and CTTU, and would supplement the work done with support from an Inter-American Development Bank (IDB) project[14] (see Table 1 below with completed and planned processes for automation). The PIU would properly monitor each activity to be financed by the Bank and by the IDB in order to avoid any financing overlap: Table 2 expresses the relationship between the two institutions in relation to these activities.

[14] The IDB project is the National Program to Support the Administration and Fiscal Management of Brazilian Municípios (*Programa Nacional de Administração Fiscal para os Municipios Brasileiros* – PNAFM), BR-L1252, approved November 30, 2009.

Table 1: List of processes automated or to be automated with support of IDB-supported Program (PNAFM)

Units	Processes
SEFIN/GOTM	1.Discharge of collection of legal persons
SEFIN/GFT	2. Fiscal notification
SEFIN/GTI	3. "Habite-se"
SEFIN/DGLC	4. Bidding process
SEFIN/GAC	5. Tax setoff
SADGP/DGCFP	6. Premium-leave 7. Retirement
SECOM	8. Publication in the Official Journal
SCDUO/CODECIR	9. Risk areas monitoring
SCDUO/DIRCON	10. Denunciation 11. Notification 12. Violation proceedings 13. Location and functioning permit
URB	14. Strategic projects management 15. Property regularization 16. Procurement 17. Budgeting and financial execution 18. Inspection and measurement 19. Environmental permits 20. Construction permits

Source: SEGESP

Table 2: Relationship between IDB-supported (PNAFM) and this Project

Sub-components covered in both projects	World Bank	IDB
a) Tax Administration	1) Selective update of IPTU's property inventory and re-assessment of property values for IPTU 2) Enhancement of voluntary tax compliance by improving SEFIN's web-based tax collection system and developing a new revenue administration system, replacing the current system *tributos municipais* 3) Strengthening of SAJ for enhancing tax debt management through purchase of management system and digitalization of legal opinions	1) IPTU: Initial work for property re-assessment (not done), support to Cadastre unit through IT and office equipment and training. 2) Enhancement of tax collection by improved management of notifications to taxpayers and IT and office equipment for the Tax Collection Unit 3) Remapping of processes for non-tax debt
b) Increasing Efficiency of public expenditures	1) Human Resources Management (HRM): Technical assistance for initial diagnostic, purchase of a new payroll management system, implementation of payroll audits and enhanced controls over personnel expenditures 2) Procurement: system for managing contracts, continuous training program, purchasing of new equipment 3) PFM: TA for continuation of cost-accounting improvements, continuous training on accounting.	1) HRM: purchase of IT and office equipment, digitalization of personnel records and training on qualifications. 2) Procurement: purchase of IT and office equipment, training, process mapping. 3) PFM: TA for budget and financial management, initiation of cost accounting efforts, IT and office equipment, and training program on budget and public policy.
c) Municipal planning and result based-management	1) Performance management: TA to set up and implementation of a Unit for Monitoring of Strategic Projects, including the development of a system of strategic indicators, and performance management training program for 200 managers and key staff 2) TA to map and automate 30 key administrative procedures	1) Information system for city planning and performance indicators through purchase of IT and office equipment for SEGESP. 2) Automation of key processes

(d) *Project management (US$2,700,000)*. This sub-component would finance activities for Project Management. The Project would finance a Project Implementation Unit (PIU), including a deputy coordinator, a procurement specialist, a financial management specialist, and five consultants to act as the focal points in the five participating entities.

The TOR and appointment of these individuals would be approved by the Bank. This activity would also finance acquisition of equipment for SEGESP and the PIU. It would also finance hiring of an IVA.

22. ***Sub-component 2(f) Urban mobility management (estimated cost US$6.4 million)***. In the beginning of 2011, the Municipal Plan for Urban Mobility was designed in Recife aiming at the improvement of urban mobility in the city. This plan seeks to improve the existing network of the Integrated Structural System (SEI), and to propose new studies on the modes of mobility in compliance with the guidelines established by the Ministry of Cities' National Policy for Sustainable Urban Transport. The Municipal Plan for Urban Mobility in Recife stresses the need for specific studies to justify and implement the main established guidelines.

23. There are several links between mobility provision and social exclusion. The negative impact of road traffic on mobility plays an important role in the exclusion of education. Inadequate access and poor mobility provision are substantial barriers to schools and are linked to young people dropping out of college.

24. The challenge to be faced in Recife´s urban mobility management is inherently related to three main problems: (a) the growth of the fleet, (b) deficiencies of road infrastructure and passengers' mobility services, and (c) institutional deficiencies.

(a) *Growth of the fleet.* Traffic congestion due to more vehicles has grown more quickly than investments in the mobility network. Recife has about 1.5 million inhabitants spread irregularly over 217 square kilometers. Over the decades, rapid urbanization has resulted in uncontrolled urban sprawl with associated traffic congestion and increasing travel distances. The problems and costs of traffic congestion in Recife affect students traveling to school, passengers, contribute negatively to the economic development and competitiveness prospects of the region, and tend to have a disproportionate impact on the poor. Each day, Recife's two subways and 354 bus lines carry 1.5 million passengers. Last year, 158,000 new cars were registered in the State of Pernambuco. In December alone, an additional 22,000 cars hit the roads of the metropolitan region of Recife. Although Recife is Brazil's second smallest state capital with 217,494 km^2, it has the sixth largest fleet of vehicles at around 500,000. Add the vehicles from the municipalities in the metropolitan region, and the number doubles.

(b) *Infrastructure for mobility network.* The arrival of the World Cup and the allocation of federal funding are seen as an opportunity to unclog traffic. According to the estimates of SSP, 35 percent and 40 percent of the private transport would migrate to the under construction expressway Via Mangue, alleviating traffic and permitting the installation of public transport corridors. Seventy kilometers of cycle lanes are expected to be built alongside these corridors. Another possibility that the Government is examining is to use the Growth Accelerated Program (*Programa de Aceleração do Crescimento* -- PAC) funding to establish alternative public transport on the Capibaribe river, towards the World Cup City in the west of Recife. The idea would be to use the river to link the city center to the nearby BR-101 highway. Projects are already in place to build more integrated passenger terminals, increasing the number from 13 to 22. The subway system is purchasing 15 new trains and building a new station, at a cost of R$15.8 million, less than one kilometer from the World Cup Stadium.

(c) *Institutional deficiencies*. CTTU does not yet have adequate information and control systems to effectively perform its functions. CTTU still needs to be strengthened through recruitment of new staff with relevant technical expertise, and through extensive training program in relevant areas.

25. Each day in Recife, 15 percent of the 1.8 million of public transport passengers are students. On their way from home to school and to work, traffic and mobility provision have direct impact on their mobility. Several factors influence the mobility of the students. Accessibility to public mobility, frequency, volume of passengers, travel time, comfort, safety, among other factors are influencing the mobility of elementary school to higher education.

26. Through prioritization of public transport and operational management, this sub-component is expected to facilitate ongoing urban mobility management, as well as mobility for students in Recife. This mobility would be achieved by improving and facilitating access to various locales for education, culture, sport, leisure, work and other activities. The Project would support two activities to ensure mobility as a facilitator for education inclusion:

- *Implementation of a traffic and transport integration data center.* A traffic and transport integration data center would maximize advantages in managing, regulating and monitoring the traffic flow and transport systems. The data is collected in real time. The data is gathered from detectors on roadways network and bus tracking system. Merging these data is expected to enhance efficiency in operating performance in the system. With the implementation of this center in Recife, the public transport system can be managed more effectively, including improving transport for students, through: (i) reliability of public transport schedule; (ii) compliance in frequency of travel; (iii) reduce travel time in Recife's main corridors; (iv) increase average speed in bus lanes; (v) reduction of irregularities in the operation; and (vi) decrease of users' complaints.

- *Preparation of Urban Plans to improve mobility in key areas of the MOR's territory, as well as design of specific investments within those Urban Plans.* Linked with the traffic and transport integration data center, two urban plans would be prepared. These two urban plans would map physical interventions to ensure the mobility of students to schools and other urban facilities. Resulting from these plans, a portfolio of preliminary projects would be developed. From this portfolio of projects, some priority projects would be selected and prepared. The priority projects would focus on efficiency gains in integrating public space and equipment for expansion of education and accessibility to public transport. Two areas were selected for the development of urban plans due to their high density (Boa Viagem and City Center). In addition to mapping and managing of students' mobility in the city, benefits may occur to the transport system and education, which include (i) increased demand of students in the transport system; (ii) increased safety and comfort; (iii) reduction of dropout in high schools; (iv) increase of high school and college attainment.

Annex 3: Implementation Arrangements

I. Project Administration Mechanisms

1. The Recife SWAp is a multi-sector Project, covering education and a wide range of public management activities. Given its nature, the Project would be implemented by five different municipal Secretariats, but also benefit several other secretariats and institutions. The five participating entities are: Special Secretariat of Management and Planning (SEGESP), Secretariat of Education (SEEL), Secretariat of Finance (SEFIN), Secretariat of Public Administration and Personnel Management (SADGP), and Secretariat of Public Services (SSP). Project activities would also benefit the Secretariat of Legal Affairs (SAJ), the General Comptroller's Office (*Controladoria Geral do Município* -- CGM), the Municipal Information Technology Company (*Empresa Municipal de Informática* - EMPREL), the Company of Urban Transport and Traffic (CTTU), and other mobility-related agencies. Thus, administration mechanisms involve a degree of complexity, but would count on a centralized coordination body and a Project Operational Manual (*Manual Operacional do Projeto* - MOP) detailing Project implementation arrangements. The following paragraphs describe the participation of each one of the participating entities and their main roles and responsibilities.

2. SEGESP has been the Bank's main interlocutor for Project preparation. It is in charge of municipal planning and management activities. SEGESP monitors the municipal strategic plan in place since the beginning of the current Administration through a management model that establishes key goals and results for each sector and related Secretariat.

3. As for the Project's purposes, SEGESP would be responsible for implementing sub-component 2(e), and for the overall Project coordination and oversight of Project implementation. SEGESP is organized into four Coordination Units; the Project would be placed at the Secretary's office and directly linked to the Mayor's office. Since it would assume a coordination role, SEGESP would host a Project Implementation Unit (PIU) for handling the additional and specialized work generated by the Project, as well as providing cross support to the other participating entities.

4. Specifically, SEGESP's main responsibilities include the following:

(a) Ensuring general coordination with the Bank, SEEL, SEFIN, SADGP, SSP and other Government stakeholders with the assistance of a PIU.
(b) Creating a Consultative Committee with structure and functions satisfactory to the Bank, as defined in the MOP.
(c) Ensuring timely implementation of all Project activities, and monitoring such activities and Project related indicators. To this end, SEGESP would organize and hold regular supervision meetings amongst all participating entities.
(d) Preparing progress and financial reports (and other Project-related documents as the case may be), as agreed in the Loan Agreement, compiling Project information and results from other participating entities. Such reports shall be in the format and content acceptable to the Bank.

(e) Developing TORs for specific public management studies, in particular those under sub-component 2 (e), managing their contracting, and overseeing study implementation, as well as follow-up to ensure appropriate implementation and dissemination of results and recommendations.
(f) Providing assistance to the participating entities on Project implementation, monitoring and supervision.
(g) Ensuring compliance with eligible activities (for example no rehabilitation is eligible if it involves expansion of the footprint of existing buildings) as well as that the related Environmental Management Framework (EMF) is observed and complied with, encompassing all activities under the selected eligible programs and not only the Bank-financed ones.
(h) Ensuring that procurement is carried out following Bank rules and procedures, including the preparation of procurement plans when applicable.
(i) Leading the preparation of an action plan in case a DLI is not accomplished.
(j) Hosting and facilitating Bank supervision missions and working with the Bank to optimize the Project's results and impact.
(k) Disseminating results in such a manner as to strengthen reform constituencies and ensure the carrying out of reforms derived from Project's studies and recommendations.

5. SEEL is responsible for offering early childhood, primary and lower secondary education, as well as providing assistance to students with special needs, providing didactic materials and school meals, promoting vocational training, and fostering cultural activities. It would be responsible for the execution of the four Eligible Expenditure Programs (EEP), and their respective *Projetos/Atividades*, that have been selected by the Government to be co-financed under Component 1 (Expand coverage of improved ECE and create conditions conducive to learning in fundamental education), and also for the execution of the sub-component 2(a).

6. Because the Project would be supporting the carrying out of existing MOR's programs, it is expected that activities would be implemented, to the extent possible, using the current structure of the SEEL. SEEL's organization structure includes eight Directorates, a Management Committee and Technical Units. However, as SEEL has no previous experience in implementing Bank-financed projects, assistance may be necessary especially for the implementation of sub-component 2 (a), in which preparation of terms of reference (TOR) for education sector studies and assessments, and hiring of consulting services would be needed, as well as for preparing and compiling Project related information and reports in a format and with content satisfactory to the Bank. Sub-component 2(a) would also include activities and resources to improve SEEL's capacity to implement their own programs.

7. The specific responsibilities to be carried out by SEEL under the Project include the following:

(a) Implementing the selected EEP and complementary ones in a timely and efficient manner in order to ensure compliance with agreed Project indicators, including the disbursement-linked ones.

(b) Monitoring the quality and timely implementation of activities by SEEL's partners, including – for example – literacy, age-grade distortion, and teacher in-service training programs conducted by Institute Ayrton Senna, and the IQE.
(c) Developing TORs for specific education studies, managing their contracting, and overseeing study implementation, as well as follow-up to ensure appropriate implementation and dissemination of results and recommendations.
(d) Putting in place sound monitoring and evaluation mechanisms to allow proper and reliable collection/generation of Project indicator data, as well as for other SEEL priority indicators.
(e) Maintain technical and political dialogue with other municipal and state stakeholders, including decision-making bodies in the education sector, required for successful Project implementation.
(f) Preparing implementation and financial reports in accordance with Bank fiduciary oversight requirements, including those related to the eligible programs (activities implemented, estimated and actual expenditures), and for the technical assistance component.
(g) Participating in the Project Consultive Committee meetings lead by SEGESP, and providing the required information as described in item (f) above, in a timely manner, to comply with the technical and legal obligations associated with the Project.
(h) Together with SEGESP and the PIU, ensuring that EMF is observed and complied with, encompassing all activities under the selected EEPs and not only the Bank-financed ones.
(i) Ensuring that procurement is carried out following Bank rules and procedures, including the preparation of procurement plans when applicable.

8. SEFIN is another participating entity for this Project, which would be responsible for carrying out sub-components 2(b) and 2(c) (Tax administration and Public debt management) and some activities under 2(d) (Increasing efficiency of public expenditure). SEFIN's organizational structure encompasses an Executive Secretariat and six Directorates, including a Procurement Directorate formed by five Bidding Committees that would be in charge of procurement responsibilities under the Project. The activities and studies to be carried out by SEFIN would benefit SAJ with respect to tax administration; the CGM with respect to control of personnel expenditures; and EMPREL with respect to improving information technology systems and equipment. It would use its own structure to coordinate all these studies and activities, and would interact with SAJ, CGM, and EMPREL for technical purposes. For these activities, SEFIN would have similar responsibilities and roles as SEEL with respect to development of TORs, contracts management and oversight of studies implementation, as well as follow-up to ensure appropriate dissemination of results and recommendations, and carrying out of needed reforms.

9. In addition, SEFIN would also be in charge of providing, in a timely manner, information to SEGESP on Project implementation progress, covering the technical and financial aspects, such as information on the percentage of aggregate budget allocation for EEP's spent, which is one of the Disbursement-Linked Indicators (DLI#1). SEGESP would also have a seat at the Project Consultative Committee to monitor the Project execution as a whole.

10. SADGP would be responsible for leading several activities in the sub-component 2(d) related to increase efficiency of public expenditure. Its roles and responsibilities would be similar to SEEL and SEFIN. Since this area requires substantial reforms, SADGP would dialogue with important stakeholders, SEFIN and SEGESP to help ensure proper implementation and achievement of expected results.

11. The SSP would be responsible for the implementation of sub-component 2(f), carrying out the Project-financed urban mobility management studies, benefitting the SSP itself and also CTTU, the Recife City Institute (*Instituto da Cidade do Recife Engenheiro Pelópidas Silveira)*, and the Greater Recife Consortium on Transport (*Consórcio Grande Recife*). The SSP's organizational structure includes an Executive Secretariat, the CTTU, Management Units for building maintenance and for supervision, and two Directorates for administrative issues and for development of projects. Like SEEL and SEFIN, the SSP would have the same roles and responsibilities with respect of implementing, monitoring and supervising their activities and studies under sub-component 2(f). In addition, SSP would work closely with CTTU to conduct its activities.

12. The Project description section in this PAD describes the studies and activities to be conducted under Components 1 and 2 and by each one of the Secretariats listed above as participating entities – SEEL, SEGESP, SEFIN, SADGP and SSP.

13. *PIU*. The PIU would be located at SEGESP and staffed with technical and operational staff with TORs and qualifications acceptable by the Bank. This Project would finance a deputy coordinator, a procurement specialist, a financial management specialist, and five consultants to act as focal points in the five participating entities. The MOR would also support, as part of the PIU, an overall Project coordinator, a financial coordinator, and two support staff. The key staff (at least the deputy coordinator, a procurement specialist, a financial management specialist, and at least three focal points) would be in place not later than two (2) months after the Effectiveness date and would be kept throughout Project implementation.

14. *Project Operational Manual*. A draft MOP acceptable to the Bank, detailing functions and responsibilities for Project implementation, was a condition for Project Negotiations. Such MOP includes the relevant information for Project execution, including procurement and disbursement rules, legal covenants, flow of documents, flow of funds, safeguards-related documents, forms, manuals, standard documents, and other tools for day to day activities. The MOR and the Bank agreed that the MOP may be updated from time to time in a manner acceptable to the Bank.

II. Financial Management, Disbursements and Procurement

A. Financial Management

15. The financial management aspects of the Project would be managed by SEGESP where a PIU would be created and properly staffed. It would be responsible for the various supporting FM tasks (to be detailed in the MOP) and for assuring a smooth flow of information and

observance of Project arrangements within all other participating entities and SEFIN, responsible for supplying the budget expenditure data that would be needed for disbursements.

Conclusions of the FM assessments and disbursement arrangements

16. The assessment covered staffing, budgeting, accounting, financial reporting, auditing, and internal controls. The conclusion of the assessment is that the financial management arrangements when in place would meet the Bank's minimum requirements under OP/BP10.02 (Financial Management). The MOR has already established a well-functioning financial management system, and following the completion of the action plan proposed in this assessment, it would have in place adequate financial management arrangements, meeting the Bank fiduciary requirements. The financial management risk of the Project has been assessed at High given the MOR's challenges and the Project implementation arrangements of the Project which includes different budget executors with low institutional capacity and week internal control adherence.

Table 1: Financial Management Assessment and Risk Ratings

	Risk Rating	*Risk Mitigating Measures*	*Residual Risk*
INHERENT RISKS			
Country level	M		
Sub-national (state) level	M	PFM review conclusions were positive; however this is the first operation to use Recife PFM systems.	M
Entity level			
Implementation arrangements involve different secretariats with no experience with external financed projects. PIU not created	H	Arrangements, including Bank capacity-building activities, would be made with the participating entities for undertaking the financial management aspects of the Project.	H
Project level	H		H
OVERALL INHERENT RISK			
CONTROL RISKS			
Budget	H	Observance of minimum 60% of budgetary execution and disbursement based on actual expenditures would serve as an incentive to allocate sufficient resources	M
Accounting	M	Proper accounting function and monitoring of monthly balances of government accounts. MOR System SOFIN to be enhanced during Project execution on reporting of education sector.	M
Internal Controls	H	The CGM is newly reorganized and is not properly staffed nor carries out regular internal control reviews (financial and compliance). MOR to assure observance of policies and regulations, including proper staffing arrangements and adherence of TCE's recommendation. The internal control challenges to be faced under this Project are going to be significant. However these challenges would fall primarily under the purview of SEGESP. A MOP is being prepared for the Project that would outline the procedures to be followed. Periodic reviews of the process under the Project shall be undertaken by the Internal CGM and TCE.	H
Funds flow	M	Treasury management and centralization of disbursements from the single treasury account using standard SEFIN disbursement processes.	M
Financial Reporting	M	Regular financial reporting modified for the multi-year (Project-to-date) Project reporting requirement and Project disbursement indicators. Calculation of disbursement indicators would be closely supervised by the Bank	M
Auditing	M	TCE-PE to participate on FM capacity building training offered by the WB.	M
OVERALL CONTROL RISK	**H**		**M**
RESIDUAL RISK RATING	**M**		**M**

Staffing

17. The financial management functions would be spread over the different participating entities, and be undertaken by qualified professionals that understand Bank policies and procedures and posses the education levels, experience, and knowledge to adequately execute them. The PIU would include two staff responsible for the various supporting FM tasks (a financial management specialist and a financial coordinator) and for assuring a smooth flow of information and observance of Project arrangements within all Project executors, reporting and disbursements. The PIU would be created and staff trained on Bank FM arrangements in the early stages of Project implementation. It might experience a learning curve in managing at the start of the Project. This risk is considered high due the weak internal control arrangements, high staff turnover and the Project implementation arrangements which fiduciary functions are spread over the secretariats involved, deeming a close support by the Bank.

Budgeting

18. The MOR follows: (a) the National Accounting Standards Applicable to the Public Sector (*Normas Brasileiras de Contabilidade Aplicadas ao Setor Público* -- NBCASP), Law 4320/64 that establishes certain high-level accounting principles; and (b) the Accounting Manual Applicable to the Public Sector (*Manual de Contabilidade Aplicada ao Setor Público* -- MCASP), issued under Law 10180 of February 6, 2001 and Decree 3589 of September 6, 2001. The Project requires adherence to the first set of NBCASP and the revised MCASP issued under *Portaria* STN 467 of August 6, 2009 beginning with Fiscal Year 2013. The last Country Financial Accountability Assessment (CFAA) for Brazil indicated that law 4320/64 was in line with international accounting standards.

19. The budget cycle includes planning and implementation of all government activities, which are to be reflected in the PPA, LDO, and LOA. All accounting records are kept by the SEFIN. The PFM system (SOFIN) is used by all municipal institutions that receive/transfer government funds. MOR accounting management is under the responsibility of SEFIN. Each participating entity has a Sector Administrative Directorate (*Diretoria de Administração Setorial* -- DAS) responsible to approve the respective payments, assuring observance of the LOA. Project execution should observe budgetary law and respective procedures. The Project annual budgeting would be based on the budget execution for Component 1 and procurement plan for Component 2, which would be regularly updated in the process of implementation. The annual budgets would be prepared by each participating entity, consolidated and submitted to SEFIN. The approved annual budget would then be entered into the accounting system and used for periodic comparison with actual results as part of the interim reporting. The updated "percentage of aggregate budget allocation for EEPs spent" (budgetary execution figures of the combined budgets for the EEP to be supported under the Project) would form the basis of disbursements (see paragraph below).

Accounting System and Records

20. The accounting for both Project components would utilize the Government financial management system – SOFIN, as disbursements for Component 1 of the Project would be based on a budget line representing expenditures paid during the reporting period. While preparing accounting and financial information, transactions under both Components would be recorded as paid, and all primary supporting documentation would be maintained to facilitate ex post reviews and the annual external audits. Such documents should be maintained for a minimum period of five years.

Internal Controls

21. Internal control reviews revealed significant internal control lapses in the programs and made a number of recommendations for improvement relating to eligibility criteria and allocation policies, documentation and reports, payment procedures and administrative controls. Although a CGM has been created (subordinated to the Mayor Office), it is not properly staffed and does not have clear and transparent policies and procedures[15]. SEGESP agreed to follow up with the CGM on the Pernambuco State Court of Accounts – *Tribunal de Contas do Estado*, or TCE-PE for addressing the recommendations and developing an action plan to strengthen it and to be supported throughout Project implementation. It has been agreed that during Project implementation the CGM shall be properly staffed and periodically review the expenditures under the budget line to be established and attainment of the milestones and disbursement targets to be agreed under the Project.

22. Flow chart of the payment cycle, including documentation and reconciliation aspects, of the EEP was prepared to avoid lapses, duplication and redundancy in the current payment and documentation processes. A review of the current payment and documentation processes would facilitate not only the streamlining of the payment procedures, but would also facilitate the closing of any current gaps in the process and the amelioration of current deficiencies.

23. The MOP would document these Project processes, and serve as an important source for processing steps to be followed during Project implementation. It would contain detailed procedures and guidelines for disbursements, payments, approvals, commitments, payments and reporting.

Interim and Annual Reporting

24. All FM information would be consolidated by SEGESP through the PIU (including receiving from SEEL the report confirming achievement of agreed milestones, which would be responsible for submitting to the Bank the Interim Un-audited Financial Reports (IFRs), by component, budget line and activity, for both monitoring and disbursements purposes. The formats of the IFRs follow the format of the existing Government reporting to the extent possible. For financial management monitoring reasons, the PIU would prepare consolidated IFRs (1-A - source and use of funds by category and 1-B – investment by components) in the currency of the Designated Account on a cash accounting basis and submit them to the Bank, no

[15] Outlined at the latest audit report issued by TCE-PE and confirmed during the FMA.

later than two (2) months after the end of each semester. The IFRs would state the expenditure figures by semester, accumulated for the year and accumulated for the loan and would be jointly sent with Component 1 reports for disbursement purposes (IFR 1-C percent of EEP budget execution threshold and DLI) and subject to Bank supervision, CGM and External Auditors reviews.

25. For disbursement purposes of Component 1, an additional report (IFR 1-C) would show achievement of the agreed Disbursement-Linked Indicators (DLI) and would be submitted 60 days after the end of each calendar semester assuring prior approval by the Bank. Some DLIs, as described in their protocols, would also be subject to clearance by an IVA, which would take place at least twice during Project life (no later than the sixth Loan withdrawal and the eleventh Loan withdrawal), as agreed by the MOR and the Bank. The description of the IFRs would be attached to the Disbursement Letter and would be included in the MOP.

26. In agreement between the Bank and the MOR, the reports indicated below can be adjusted during Project implementation:

- IFR 1-A: Statement of Sources and Uses of Funds, by Project category: EEP and Component 2, respectively; cumulative (For the previous semester; year-to-date; and Project to date) and for the last period.
- IFR 1-B: Statement of Investment by Project budget line, components and sub-component, cumulative (For the previous semester; year-to-date; and Project to date), showing updated budgeted (LOA) amounts versus actual expenditures, (i.e., documented expenditures), including a variance analysis.
- IFR 1-C: Percentage (60 percent) of aggregate budget allocation for EEPs spent and achievement of other agreed DLIs. Reconciliation of the Designated Account (attaching bank account statements).

External Audit Arrangements

27. The Pernambuco State Court of Accounts – *Tribunal de Contas do Estado*, or TCE-PE – has adequate capacity and staff to fulfill its mandate to audit the State's and MOR's accounts. The TCE-PE has established audit guidelines and regulations in place and the scope of the TCE-PE audits include financial and operational audits, evaluation of internal controls and compliance with laws, rules and regulations, among other audit and review functions.

28. The MOR, through SEGESP, would submit a formal written request to the TCE-PE each year, asking for a copy of the annual audit report. Specifically, the formal request would solicit a copy of the audit opinion and the summary report. In case the Project audit is not carried out by TCE-PE, such audit would be undertaken by a private independent firm. The Bank expects to receive a copy of the audit report on the Project by June 30 of each year.

Financial Management Supervision Arrangements

29. As part of its Project supervision missions, the Bank would conduct risk-based financial management supervision, at appropriate intervals. These would pay particular attention to: (a)

Project accounting and internal controls (rated as High risk), (b) budgeting and financial planning arrangements; (c) review of the Interim Un-audited Financial Reports; (d) review of audit reports including financial statements and remedial actions recommended in the auditor's Management Letters; (e) disbursement management and financial flows, including counterpart funds, as applicable; and (f) any incidences of corrupt practices involving Project resources. Proposed supervision interval for this Project is at least twice a year.

Table 2: Financial Management Action Plan

#	Proposed Action	Responsible Party	Date of Completion
1	Hire key PIU staff	SEGESP	Up to two (2) months after Effective Date
2	Budget preparation (LOA) and respective update at SOFIN to follow Project designs (component and sub-component)	SEGESP	By negotiations (completed) and throughout Project life
3	Develop Plan of Action to address recommendations of the Reviews of TCE	SEGESP and CGM	By negotiations (completed) and throughout Project life
4	Prepare Flow of Funds Chart, update Payment Cycles, including documentation and reconciliation processes for both components	SEGESP	Appraisal (completed)
5	Determine Milestone and Targets for Disbursements under Component 1	SEGESP	Appraisal (completed)
6	Project Operational Manual	SEGESP	By negotiations (completed)
7	Selection of the IVA to verify that Milestone and Targets have been attained	SEGESP	According to agreed schedule
8	Confirm inclusion of Project processes on its annual review of its work program	CGM	By negotiations (completed) and throughout Project life
9	Prepare the external auditors TCE-PE TOR	SEGESP/ BANK	1st quarter of Project implementation
11	Open Designated Account	SEGESP / SEFIN	Signing
12	IFRs templates	SEGESP / BANK	By negotiations (completed)

Addressing Capacity Constraints

30. Two main areas were identified in terms of implementation capacity, namely administrative capacity constraints and financial management constraints. The planned establishment of a PIU under SEGESP to manage both components is a direct response to administrative capacity concerns. The management of the SOFIN system further highlighted a need to address the MOR information management capacity. The hiring of two FM staff within the PIU and focal points to support the implementing secretariats would enable the attention to detail necessary for effective management of the system and support other participating entities. Financial support from the PIU is essential with limited staffing in the financial area at SEGESP's disposal.

B. Disbursements

31. The Project has different disbursement arrangements for each one of its components. Under Component 1 (SWAp), the Project would co-finance the selected EEP and reimburse the

MOR against the presentation of eligible expenditures, but also would take a results-based financing approach to the implementation of agreed activities and policies not only in the Education sector but also in public management. Thus, under this Component, SEEL, SEFIN, SADGP and SEGESP are expected to achieve specific results, which would then contribute to trigger disbursements. The Project preparation team has selected 12 DLIs (8 Education, two public management, one related to overall budget execution, and one institutional related) that are likely to be challenging but realistic and that support the achievement of the Project Development Objective (PDO). On the other hand, disbursements for Component 2 would be made through Advances to a Designated Account. Thus, two separate Withdrawal Applications would need to be submitted each time a disbursement is requested – a Reimbursement Withdrawal Application for Component 1 (attaching IFRs), and an Advance Withdrawal Application for Component 2 (attaching Statement of Expenditures and other necessary documentation). Details of disbursement arrangements by components are described in the following paragraphs.

32. Under Component 1, disbursements would be made according to the following mechanisms:

- Disbursements would be made against the SEEL's four pre-defined EEPs.[16] The loan disbursements would be tagged in the SEEL's budget system as co-financing the EEPs but funds would flow to the MOR's Treasury. In addition, loan funds may also be tagged in other municipal Secretariats' budgets depending on the use of such funds once reimbursed.
- Each year SEEL would budget and approve each EEP, as well as assign to each EEP the same budget code used in the Multi-Year Plan for 2010-2013 as indicated in the EEP table (Table 5). The budgeted amounts are expected to be at least the ones indicated in the EEP table, but SEGESP (with assistance of SEEL and SEFIN) and the Bank may adjust, once every year, the amounts assigned per budget code to the EEPs in a manner satisfactory to the Bank. The Government's financial systems (SOFIN) would track and report budget estimates and actual expenditures, which means that the Government's financial systems would be used for purposes of Project financial management, instead of developing a new system only for the purposes of monitoring the Project.
- As per the SWAp characteristics, the Bank finances a percentage against the aggregate EEP expenditures and not a percentage of a transaction (or contract) as in traditional specific investment loans. In this case, a financing percentage up to 30 percent has been agreed upon and would form the upper limit for the amount to be disbursed against aggregate EEP expenditures. Thus, to disburse an amount that represents 30 percent of the aggregate EEP expenditures, the MOR should present such amount times 3.33 in expenditures under the EEP, out of which at least 30 percent (the agreed percentage of financing) must comply with Project's procurement rules to be eligible for financing.[17]

[16] The four EEPs are: 1206 – Effective Organization for Teaching and Learning; 1207 – Effective Support for Quality Education; 1214 – Social Assistance to the Municipal Students; and 2110 – Management of the Education Municipal Policies.

[17] For instance, to disburse US$10 million, the MOR shall present US$33.33 million in expenditures under the EEP, where at least US$10 million shall comply with the Bank's procurement rules to be eligible for financing.

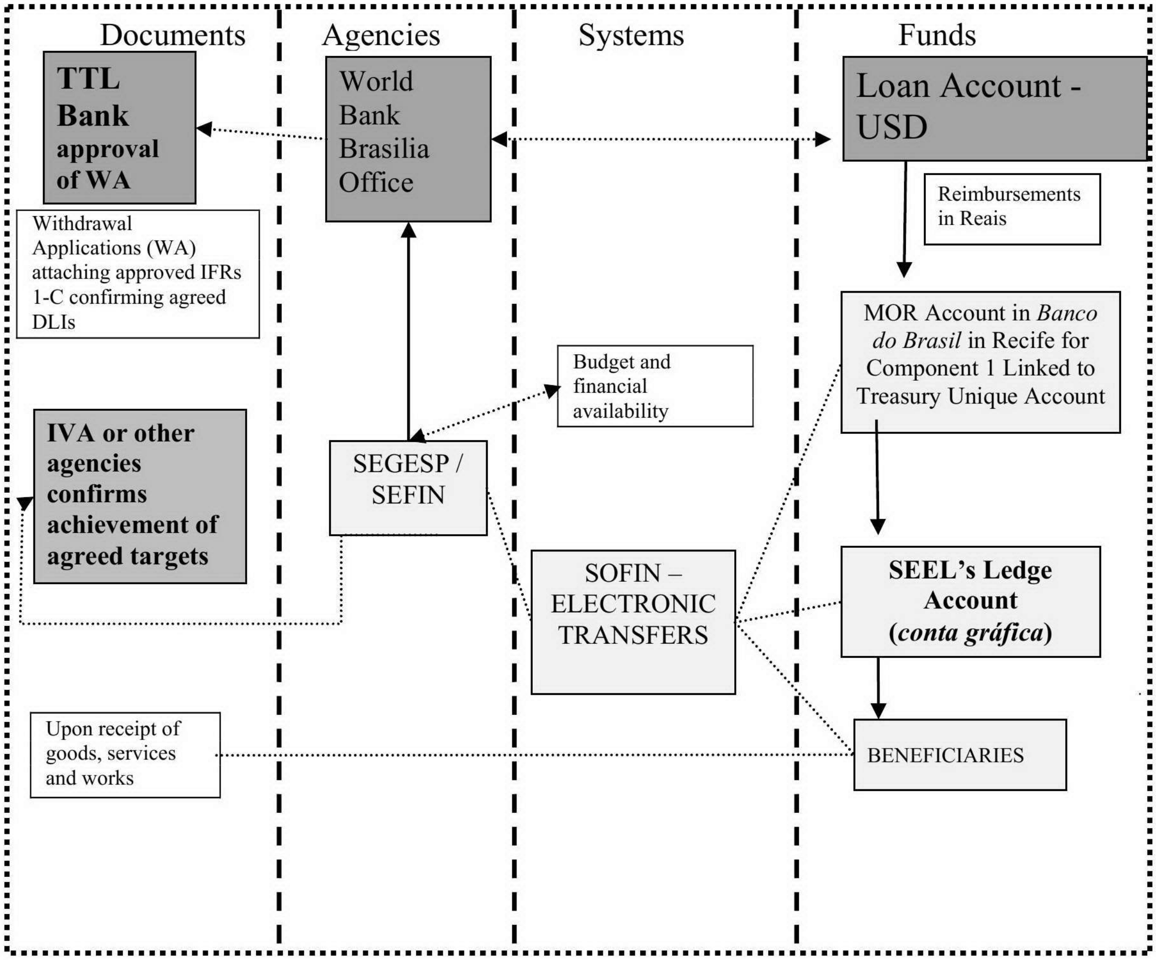
- In order to comply with the 30 percent requirement, the MOR would present, prior to the disbursements take place, a list of (a) contracts that follow procurement rules as described in the Loan Agreement, (b) non-procurable expenditures, and (c) selected recurrent expenditures. The list of expenditures would be in a format acceptable and cleared by the Bank, as well as subject to the financial audits by TCE (or any other agency acceptable to the Bank) as other Project's expenditures. This list could also be part of the Project Reports to be submitted each semester.
- Disbursements would be made in 11 reimbursements for actual EEP expenditures through the submission of IFRs. The 1st reimbursement may take place after loan Effectiveness (expected to be September 3, 2012) as retroactive financing, and, as such, would cover the period up to 12 months prior to the Loan Agreement date (but on or after July 1, 2011) and would not exceed US$19.8 million, not to exceed a total of US$20 million between Component 1 and Component 2. The potential expenditures to be retroactively financed, under Component 1, would include: (a) contracts that comply with Bank procurement rules, including the anti-corruption clauses; (b) non-procurable items such as *Bolsa Escola* (student grants), and *Suprimento Individual* (school grants) for schools and ECE centers; and (c) selected recurrent expenditures, including those associated with the physical functioning and maintenance of municipal schools and early childhood education centers.
- The following 10 reimbursements would be made in the months of March and September of each year, against actual expenditures for the four EEP, incurred in the previous six-month period, defined as July to December and January to June of each year of Project implementation, except for the 2nd disbursement for which period would be from loan signing date to December 31, 2012.
- The following 10 reimbursements would also take into account SEEL's, SEFIN's, SADGP's, and SEGESP's compliance with DLIs to be verified at the end of each six-month period (by December 31 and June 30 of each year) in accordance with the agreed targets and schedule for each indicator. The Project has a total of 12 DLIs out of 5 PDO Level Results Indicators and 16 Intermediate Results Indicators. Each DLI has the same weight to compose the total disbursement amount per period, and a protocol detailing how it would be measured and by which sources. Proposed disbursement amounts and rules per period take into account technical premises, and expected budget allocation and SEEL's capacity of spending. The disbursement table (Disbursement Arrangements for Component 1 -- Table 6) details the disbursement rules for each period.
- DLI#1 is the 60 percent rule, meaning that at least 60 percent of aggregate budget allocation for EEPs shall be spent in a calendar year. If SEEL fails to achieve the 60 percent target (DLI #1), the corresponding amount to be disbursed from the loan attributable to DLI #1 would be pro-rated according to the level of execution.
- If a DLI target is not fully achieved, an amount proportional to the extent to which the DLI was met would be disbursed, except for the ones that do not have quantitative targets - DLI #9, 10, 11, and 12. SEEL, SEFIN, SADGP and SEGESP, as the case may be, with assistance of the Bank, would agree on an Action Plan to ensure the DLI target is fully achieved under the Project, and the amounts withheld for each failed DLI would be paid when the DLI is fully achieved.
- MOR would select and contract an IVA, not later than 18 months after the Effectiveness, date to carry out at least two technical reviews of agreed results during Project life. The

first review should be completed not later than the 6th loan withdrawal, and the second not later than the 11th loan withdrawal – such reviews would be mandatory for the indicators subject to IVA verification, and the related disbursements would be suspended in case of non-compliance. The source of verification of each DLI is detailed at their protocols, as well as the ones which would be subject to the verification of IVA.

- Prior to the 6th disbursement, a Project Mid-Term Review (MTR) would be conducted to evaluate, among other Project aspects, the performance of the results-based framework and the accomplishment of the Project DLIs. This MTR would determine if any new or the existing DLIs would be required to be incorporated or modified in the current results-based framework in line with the disbursement mechanism/modalities used by the Project.
- Specific requirements and penalties for DLIs not met under Component 1 have been included in Table 7 of this Annex.

33. Disbursements under Component 2 of the Project would be made through advances (Withdrawal Application attaching Statement of Expenditures and other necessary documentation) provided to a Designated Account (DA) to be opened in a financial institution selected in consultation with the Bank (acceptable to the Bank). The DA, which would be segregated, would be managed by SEGESP and SEFIN in accordance with procedures established in the MOP. The DA would be in Brazilian Reais, and have a fixed ceiling of R$15,000,000. This account would be operated in accordance with the procedures and guidelines set forth in the Bank's Disbursement Handbook. As eligible expenditures are incurred, the PIU would withdraw the amount to be financed by IBRD from the Designated Account (R$) in accordance with the financing percentage agreed. Proceeds of the loan would be disbursed to the Real-denominated designated account following Effectiveness. The Disbursement Deadline Date (for receipt by the Bank of applications for withdrawal and supporting documentation) is four months after the Closing date. Given that the MOR may be initiating some activities under this Component even before the Loan Agreement signature, retroactive financing could be made, up to US$200,000, not to exceed a total of US$20 million between Component 1 and Component 2, for eligible expenditures incurred up to 12 months prior to the Loan Agreement date (but on or after July 1, 2011).

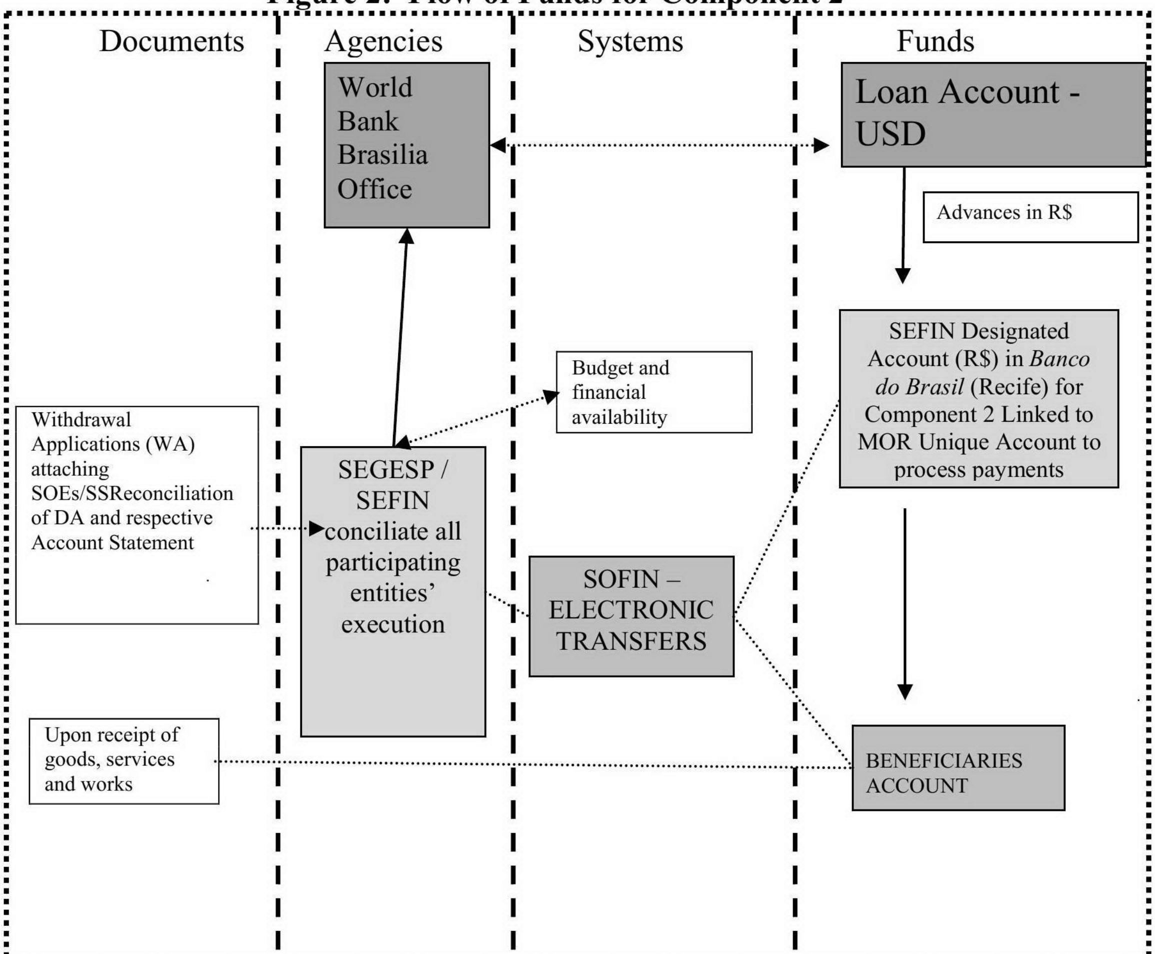
Figure 1: Flow of Funds for Component 1



- SEGESP/SEFIN prepare LOA (based on information received from SEEL) that is updated at SOFIN, which executes and accounts the MOR budget.
- SEEL updates SOFIN with respective beneficiaries' contracts and *convenios* data (e.g.: name, bank account, disbursement schedule, etc)
- Upon assurance that goods and services have been rendered, SEEL liquidates respective payments.
- SEFIN transfers respective funds from the MOR's unique account to SEEL project ledge account so that payments are electronically processed through *Banco do Basil* directly to respective beneficiary account. On a daily basis, SEEL conciliates reports generated by SOFIN and by *Banco do Brasil*.
- Budget execution means actual expenditures paid for goods and services rendered, except in case of EEP 1206 (lines 2178 and 2179) and EEP 1214 (line 2107), where part of expenditures refers to school grants (*Suprimento Individual*) to fundamental education schools and ECE centers - *creches*, pre-schools, and CMEIs; and students' grants (*Bolsa Escola*) respectively.

- Every semester, SEGESP confirms budget execution with SEEL and other participating entities, and jointly with SEFIN prepares the IFRs following agreed disbursement arrangements (including achievement of DLIs targets), which are subject to the Bank's approval prior from processing disbursements.
- IFRs would be the basis to reimburse Component 1, but would also include execution of Component 2 for monitoring and auditing purposes. Disbursement requests shall be submitted to the World Bank Disbursement Department in Brasilia.
- Loan proceeds would flow from the Loan Account to a segregated account (which is part of MOR unique account) opened to receive Component 1 reimbursements, which would be accounted following MOR's internal source of funds and accounting procedures, and would not necessarily be used to pay and account eligible expenditures under Component 1.

Figure 2: Flow of Funds for Component 2



- SEFIN would open one Designated Account (DA) under its name in the *Banco do Brasil* (Recife) in Reais to receive loan funds and process all local currency payments.
- SEGESP would consolidate data received from other participating entities, and send to SEFIN that would prepare the annual budget proposal, assure budget and financial availability which would be formally approved through the LOA.
- Each participating entity would update SOFIN with respective beneficiaries' contracts data (e.g.: name, bank account, disbursement schedule, etc)
- Upon assurance that goods and services (including selected rehabilitation) have been rendered, each Participating Entity liquidates respective payments.
- SEFIN would electronically transfer payments directly to each beneficiary account, upon proof of services rendered, operating costs incurred, and receipt (goods), by the participating entities.
- SEGESP would monitor and reconcile payments on a monthly basis through reports available at SOFIN and *Banco do Brasil*.
- Original support documentation would be kept by each participating entity and SEGESP would make them available to the CGM, external auditors and Bank upon request.
- SEGESP (through PIU) would prepare consolidated statement of expenditures (SOEs) or summary sheets attaching bank reconciliation and account statement to be submitted to the World Bank Disbursement Department in Brasília.

Table 3: Allocation of Loan Proceeds

Category	Amount of the Loan Allocated (expressed in USD)	Percentage of Expenditures to be financed (inclusive of taxes)
(1) Eligible Expenditure Programs under Component 1	100,000,000	30% of aggregate EEP expenditures
(2) Goods, consultants' services, non-consulting services, training, and operating costs under Component 2	30,000,000	100%
TOTAL AMOUNT	130,000,000	

Table 4: Summary of Estimated Disbursement Amounts by Expected Disbursement Date and Project Component

Expected Disbursement Date	Component 1	Component 2	Total
September 2012	19,800,000	300,000*	20,100,000
March 2013	11,200,000	300,000	11,500,000
September 2013	5,700,000	1,500,000	7,200,000
March 2014	11,200,000	1,500,000	12,700,000
September 2014	5,700,000	4,200,000	9,900,000
March 2015	11,200,000	4,200,000	15,400,000
September 2015	5,700,000	4,500,000	10,200,000
March 2016	11,200,000	4,500,000	15,700,000
September 2016	5,700,000	4,500,000	10,200,000
March 2017	6,900,000	4,500,000	11,400,000
September 2017	5,700,000	0	5,700,000
Total	**100,000,000**	**30,000,000**	**130,000,000**

* This amount includes: (i) possible retroactive financing in the total amount of US$200,000; and (ii) advance in the total amount of US$100,000.

Table 5: Eligible Expenditures Programs (EEP)
(Expressed in R$)

Budget Code and Programs[A]	2011[B]	2012[C]	2013[D]	2014[D]	2015[D]	2016[D]	2017[D]	Total
1206 – Effective Organization for Teaching and Learning								
2.101 - Implementation of continued training policies for municipal teachers.	4,999,328	1,940,000	2,027,300	2,118,529	2,213,862	2,313,486	2,417,593	**18,030,098**
2.125 – Increase and improvement of quality of IT and communication processes in the education municipal network.	412,000	850,000	888,250	928,221	969,991	1,013,641	1,059,255	**6,121,358**
2.178 – Increase of coverage and improvement of quality of primary education.	90,677,598	87,070,000	90,988,150	95,082,617	99,361,335	103,832,595	108,505,061	**675,517,355**
2.179 - Increase of coverage and improvement of quality of early childhood education.	9,801,644	11,640,000	12,163800	12,711,171	13,283,174	13,880,917	14,505,558	**87,986,263**
2.182 - Implementation of mechanisms for school inclusion of students with special learning needs (including *Bolsa Escola* Program and School Grants).	140,000	1,930,000	2,016,850	2,107,608	2,202,451	2,301,561	2,405,131	**13,103,601**
Subtotal	**106,030,570**	**103,430,000**	**108,084,350**	**112,948,146**	**118,030,812**	**123,342,199**	**128,892,598**	**800,758,675**
1207- Effective Support for Quality Education								
2.128 - Provision of school furniture, equipment and supplies.	5,161,482	5,000,000	5,225,000	5,460,125	5,705,831	5,962,593	6,230,910	**38,745,940**
2.131 – Rehabilitation and maintenance of the municipal education infrastructure.	10,962,000	11,100,000	11,599,500	12,121,478	12,666,944	13,236,956	13,832,620	**85,519,497**
Subtotal	**16,123,482**	**16,100,000**	**16,824,500**	**17,581,603**	**18,372,775**	**19,199,549**	**20,063,529**	**124,265,438**

Budget Code and Programs[A]	2011[B]	2012[C]	2013[D]	2014[D]	2015[D]	2016[D]	2017[D]	Total
1214 – Social Assistance to the Municipal Students								
2.107 - Development of supplementary programs for the municipal education.	65,967,322	70,000,000	73,150,000	76,441,750	79,881,629	83,476,302	87,232,736	536,149,738
Subtotal	**65,967,322**	**70,000,000**	**73,150,000**	**76,441,750**	**79,881,629**	**83,476,302**	**87,232,736**	**536,149,738**
2110 – Management of the Education Municipal Policies								
2.035 - Coordination and supervision of education and sports policies.	319,972	860,000	898,700	939,142	981,403	1,025,566	1,071,716	6,096,499
Subtotal	**319,972**	**860,000**	**898,700**	**939,142**	**981,403**	**1,025,566**	**1,071,716**	**6,096,499**
TOTAL	**188,441,346**	**190,390,000**	**198,957,550**	**207,910,640**	**217,266,619**	**227,043,616**	**237,260,579**	**1,467,270,350**

[A] Such programs and respective *Projetos/Atividades* (each line of the above table) include investment and selected recurrent expenditures. The nature of investment expenditures includes, *inter alia*, selected rehabilitation of schools and early child education centers; school furniture, books and other learning materials; supplies; services; hiring of individuals and firms, universities and other institutions; rental costs; logistics; training costs; school grants; student grants; and maintenance costs.

[B] LOA 2011 including supplemental funds up to November 18, 2011.

[C] PPA and LOA 2012 submitted to Municipal Council on September 30, 2011.

[D] Forecasts based on LOA 2011 with 4.5 percent inflation added to each year.

Table 6: Disbursements Arrangements for Component 1

No.	Project Disbursement Timing	Disbursement Type	Estimated amount		DLI	Date DLI would be measured	Information to be provided by the MOR
			%	Amount (US$M)			
1st DISBURSEMENT – US$19.8 MILLION							
1	September 2012	1st reimbursement of EEP expenditures (retroactive financing)	100	19.800	No DLIs are expected to be achieved for the retroactive financing	N/A	Actual EEP expenditures incurred and paid up to 12 months before the expected loan signing, in a total amount not less than US$66.000 million out of which at least US$19.800 million shall comply with Bank criteria and procurement rules to be considered eligible for Bank financing.
2nd DISBURSEMENT – US$11.2 MILLION							
2	March 2013	2nd reimbursement of EEP expenditures					Actual EEP expenditures incurred and paid for the period from loan signing to December 31, 2012, in a total amount not less than US$37.334 million in which at least US$11.2 million shall comply with Bank criteria and procurement rules to be considered eligible for Bank financing.
			16.667	1.867	Percentage of aggregate budget allocation for EEPs spent (DLI 1)	December 31, 2012	At least 60%. Information for January 1, 2012 to December 31, 2012.
			16.667	1.867	Percentage of all early child education facilities with emergency needs (first number) and priority needs (second number) that received required rehabilitation (DLI 4)	December 31, 2012	100% of emergency needs and 80% of priority needs.
			16.667	1.867	Number of early child education professionals who received in-service training (DLI 6)	December 31, 2012	At least 1,050 professionals participated in at least 20 hours of in-service training, with documentation of participants and specific courses

No.	Project Disbursement Timing	Disbursement Type	Estimated amount		DLI	Date DLI would be measured	Information to be provided by the MOR
			%	Amount (US$M)			
			16.667	1.867	Percentage of teachers, directors, and pedagogical coordinators in fundamental education who received in-service training (DLI 7)	December 31, 2012	At least 75% of professionals participated in at least 20 hours of in-service training, with documentation of participants and specific courses
			16.667	1.867	Number of schools that received systematic follow-up on management plan from the Core Regional Follow-up team (DLI 8)	December 31, 2012	At least 70 schools received follow-up, with documentation in the form of monitoring reports and school management plans for that year for each school.
			16.665	1.867	Maintain key staff (DLI 12)	December 31, 2012	At least the deputy coordinator, a procurement specialist, a financial management specialist, and at least three focal points, with experience and functions acceptable by the Bank, have been selected, hired, and are working in the Project.
3rd DISBURSEMENT – US$5.7 MILLION							
3	September 2013	3rd reimbursement of EEP expenditures					Actual EEP expenditures incurred and paid for the period from January 1, 2013 to June 30, 2013, in a total amount not less than US$19.000 million out of which at least US$5.700 million shall comply with Bank criteria and procurement rules to be considered eligible for Bank financing.
			16.667	0.950	Number of students enrolled in extended school day program (DLI 3)	June 30, 2013	At least 2,450 children enrolled, verified by enrollment records
			16.667	0.950	Number of students in Grades 1-5 enrolled in accelerated learning programs (DLI 5)	June 30, 2013	At least 1,900 students enrolled, as verified by enrollment records
			16.667	0.950	System for learning	June 30, 2013	System functioning at Level 1 of utility.

No.	Project Disbursement Timing	Disbursement Type	Estimated amount		DLI	Date DLI would be measured	Information to be provided by the MOR
			%	Amount (US$M)			
					assessment at the primary level (SMAR) (DLI 9)		
			16.667	0.950	Quality of Recife's tax administration system (DLI 10)	June 30, 2013	TOR for firm to carry out property reassessment approved by Bank
			16.667	0.950	Efficiency of payroll management (DLI 11)	June 30, 2013	TORs for payroll audit and new payroll system approved by WB
			16.667	0.950	Maintain key staff (DLI 12)	June 30, 2013	At least the deputy coordinator, a procurement specialist, a financial management specialist, and at least three focal points, with experience and functions acceptable by the Bank, have been selected, hired, and are working in the Project.
4th DISBURSEMENT – US$11.2 MILLION							
4	March 2014	4th reimbursement of EEP expenditures					Actual EEP expenditures incurred and paid for the period July 1, 2013 to December 31, 2013, in a total amount not less than US$37.334 million in which at least US$11.200 million shall comply with Bank criteria and procurement rules to be considered eligible for Bank financing.
			14.286	1.600	Percentage of aggregate budget allocation for EEPs spent (DLI 1)	December 31, 2013	At least 60%. Information for January 1, 2013 to December 31, 2013.
			14.286	1.600	Percentage of all early child education facilities with emergency needs (first number) and priority needs (second number) that received required rehabilitation (DLI 4)	December 31, 2013	100% of emergency needs and 80% of priority needs.

No.	Project Disbursement Timing	Disbursement Type	Estimated amount		DLI	Date DLI would be measured	Information to be provided by the MOR
			%	Amount (US$M)			
			14.286	1.600	Number of early child education professionals who received in-service training (DLI 6)	December 31, 2013	At least 1,150 professionals participated in at least 20 hours of in-service training, with documentation of participants and specific courses
			14.286	1.600	Percentage of teachers, directors, and pedagogical coordinators in fundamental education who received in-service training (DLI 7)	December 31, 2013	At least 78% of professionals participated in at least 20 hours of in-service training, with documentation of participants and specific courses
			14.286	1.600	Number of schools that received systematic follow-up on management plan from the Core Regional Follow-up team (DLI 8)	December 31, 2013	At least 85 schools received follow-up, with documentation in the form of monitoring reports and school management plans for that year for each school.
			14.286	1.600	Quality of Recife's tax administration system (DLI 10)	December 31, 2013	New web-based system for IPTU collection fully functional
			14.286	1.600	Maintain key staff (DLI 12)	December 31, 2013	At least the deputy coordinator, a procurement specialist, a financial management specialist, and at least three focal points, with experience and functions acceptable by the Bank, have been selected, hired, and are working in the Project.
5th DISBURSEMENT – US$5.7 MILLION							
5	September 2014	5th reimbursement of EEP expenditures					Actual EEP expenditures incurred and paid for the period from January 1, 2014 to June 30, 2014, in a total amount not less than US$19.000 million out of which at least US$5.700 million shall comply with Bank criteria and procurement rules to be considered eligible for Bank financing.

No.	Project Disbursement Timing	Disbursement Type	Estimated amount		DLI	Date DLI would be measured	Information to be provided by the MOR
			%	Amount (US$M)			
			16.667	0.950	Number of children enrolled in multi-sectoral ECD program (DLI 2)	June 30, 2014	At least 400 children enrolled, verified by enrollment records.
			16.667	0.950	Number of students enrolled in extended school day program (DLI 3)	June 30, 2014	At least 3,450 children enrolled, verified by enrollment records
			16.667	0.950	Number of students in Grades 1-5 enrolled in accelerated learning programs (DLI 5)	June 30, 2014	At least 1,450 students enrolled, as verified by enrollment records
			16.667	0.950	System for learning assessment at the primary level (SMAR) (DLI 9)	June 30, 2014	System functioning at Level 2 of utility.
			16.667	0.950	Efficiency of payroll management (DLI 11)	June 30, 2014	Completion of payroll audit and identification of potential savings
			16.667	0.950	Maintain key staff (DLI 12)	June 30, 2014	At least the deputy coordinator, a procurement specialist, a financial management specialist, and at least three focal points, with experience and functions acceptable by the Bank, have been selected, hired, and are working in the Project.
6th DISBURSEMENT – US$11.2 MILLION							
6	March 2015	6th reimbursement of EEP expenditures					Actual EEP expenditures incurred and paid for the period July 1, 2014 to December 31, 2014, in a total amount not less than US$37.334 million in which at least US$11.200 million shall comply with Bank criteria and procurement rules to be considered eligible for Bank financing.
			14.286	1.600	Percentage of aggregate budget allocation for EEPs spent (DLI 1)	December 31, 2014	At least 60%. Information for January 1, 2014 to December 31, 2014.
			14.286	1.600	Percentage of all early child education	December 31, 2014	100% of emergency needs and 80% of priority needs.

No.	Project Disbursement Timing	Disbursement Type	Estimated amount		DLI	Date DLI would be measured	Information to be provided by the MOR
			%	Amount (US$M)			
					facilities with emergency needs (first number) and priority needs (second number) that received required rehabilitation (DLI 4)		
			14.286	1.600	Number of early child education professionals who received in-service training (DLI 6)	December 31, 2014	At least 1,250 professionals participated in at least 20 hours of in-service training, with documentation of participants and specific courses
			14.286	1.600	Percentage of teachers, directors, and pedagogical coordinators in fundamental education who received in-service training (DLI 7)	December 31, 2014	At least 80% of professionals participated in at least 20 hours of in-service training, with documentation of participants and specific courses
			14.286	1.600	Number of schools that received systematic follow-up on management plan from the Core Regional Follow-up team (DLI 8)	December 31, 2014	At least 100 schools received follow-up, with documentation in the form of monitoring reports and school management plans for that year for each school.
			14.286	1.600	Quality of Recife's tax administration system (DLI 10)	December 31, 2014	Completion of the property reassessment
			14.286	1.600	Maintain key staff (DLI 12)	December 31, 2014	At least the deputy coordinator, a procurement specialist, a financial management specialist, and at least three focal points, with experience and functions acceptable by the Bank, have been selected, hired, and are working in the Project.

No.	Project Disbursement Timing	Disbursement Type	Estimated amount		DLI	Date DLI would be measured	Information to be provided by the MOR
			%	Amount (US$M)			
7th DISBURSEMENT – US$5.7 MILLION							
7	September 2015	7th reimbursement of EEP expenditures					Actual EEP expenditures incurred and paid for the period from January 1, 2015 to June 30, 2015, in a total amount not less than US$19.000 million out of which at least US$5.700 million shall comply with Bank criteria and procurement rules to be considered eligible for Bank financing.
			16.667	0.950	Number of children enrolled in multi-sectoral ECD program (DLI 2)	June 30, 2015	At least 800 children enrolled, verified by enrollment records.
			16.667	0.950	Number of students enrolled in extended school day program (DLI 3)	June 30, 2015	At least 3,950 children enrolled, verified by enrollment records
			16.667	0.950	Number of students in Grades 1-5 enrolled in accelerated learning programs (DLI 5)	June 30, 2015	At least 1,300 students enrolled, as verified by enrollment records
			16.667	0.950	System for learning assessment at the primary level (SMAR) (DLI 9)	June 30, 2015	System functioning at Level 3 of utility.
			16.667	0.950	Efficiency of payroll management (DLI 11)	June 30, 2015	Corrective measures to address payroll audit findings are implemented, genera-ting annual savings to the MOR of at least R$ 7.2 million

No.	Project Disbursement Timing	Disbursement Type	Estimated amount		DLI	Date DLI would be measured	Information to be provided by the MOR
			%	Amount (US$M)			
			16.667	0.950	Maintain key staff (DLI 12)	June 30, 2015	At least the deputy coordinator, a procurement specialist, a financial management specialist, and at least three focal points, with experience and functions acceptable by the Bank, have been selected, hired, and are working in the Project.
8th DISBURSEMENT – US$11.2 MILLION							
8	March 2016	8th reimbursement of EEP expenditures					Actual EEP expenditures incurred and paid for the period July 1, 2015 to December 31, 2015, in a total amount not less than US$37.334 million in which at least US$11.200 million shall comply with Bank criteria and procurement rules to be considered eligible for Bank financing.
			14.286	1.600	Percentage of aggregate budget allocation for EEPs spent (DLI 1)	December 31, 2015	At least 60%. Information for January 1, 2015 to December 31, 2015.
			14.286	1.600	Percentage of all early child education facilities with emergency needs (first number) and priority needs (second number) that received required rehabilitation (DLI 4)	December 31, 2015	100% of emergency needs and 80% of priority needs.
			14.286	1.600	Number of early child education professionals who	December 31, 2015	At least 1,350 professionals participated in at least 20 hours of in-service training, with documentation of participants and specific courses

No.	Project Disbursement Timing	Disbursement Type	Estimated amount		DLI	Date DLI would be measured	Information to be provided by the MOR
			%	Amount (US$M)			
					received in-service training (DLI 6)		
			14.286	1.600	Percentage of teachers, directors, and pedagogical coordinators in fundamental education who received in-service training (DLI 7)	December 31, 2015	At least 82% of professionals participated in at least 20 hours of in-service training, with documentation of participants and specific courses
			14.286	1.600	Number of schools that received systematic follow-up on management plan from the Core Regional Follow-up team (DLI 8)	December 31, 2015	At least 115 schools received follow-up, with documentation in the form of monitoring reports and school management plans for that year for each school.
			14.286	1.600	Quality of Recife's tax administration system (DLI 10)	December 31, 2015	Implementation of property reassessment
			14.286	1.600	Maintain key staff (DLI 12)	December 31, 2015	At least the deputy coordinator, a procurement specialist, a financial management specialist, and at least three focal points, with experience and functions acceptable by the Bank, have been selected, hired, and are working in the Project.
9TH DISBURSEMENT PERIOD – US$5.7 MILLION							
9	September 2016	9th reimbursement of EEP expenditures					Actual EEP expenditures incurred and paid for the period from January 1, 2016 to June 30, 2016, in a total amount not less than US$19.000 million out of which at least US$5.700 million shall comply with Bank criteria and procurement rules to be considered eligible for Bank financing.

No.	Project Disbursement Timing	Disbursement Type	Estimated amount		DLI	Date DLI would be measured	Information to be provided by the MOR
			%	Amount (US$M)			
			16.667	0.950	Number of children enrolled in multi-sectoral ECD program (DLI 2)	June 30, 2016	At least 1,200 children enrolled, verified by enrollment records.
			16.667	0.950	Number of students enrolled in extended school day program (DLI 3)	June 30, 2016	At least 3,950 children enrolled, verified by enrollment records
			16.667	0.950	Number of students in Grades 1-5 enrolled in accelerated learning programs (DLI 5)	June 30, 2016	At least 1,200 students enrolled, as verified by enrollment records
			16.667	0.950	System for learning assessment at the primary level (SMAR) (DLI 9)	June 30, 2016	System functioning at Level 4 of utility.
			16.667	0.950	Efficiency of payroll management (DLI 11)	June 30, 2016	New payroll system fully functional
			16.667	0.950	Maintain key staff (DLI 12)	June 30, 2016	At least the deputy coordinator, a procurement specialist, a financial management specialist, and at least three focal points, with experience and functions acceptable by the Bank, have been selected, hired, and are working in the Project.
10TH DISBURSEMENT PERIOD – US$6.9 MILLION							
10	March 2017	10th reimbursement of EEP expenditures					Actual EEP expenditures incurred and paid for the period from July 1, 2016 to December 31, 2016, in a total amount not less than US$23.000 million in which at least US$6.900 million shall comply with Bank's criteria and procurement rules to be considered eligible for Bank financing.
			16.667	1.150	Percentage of aggregate budget allocation for EEPs spent (DLI 1)	December 31, 2016	At least 60%. Information for January 1, 2016 to December 31, 2016.
			16.667	1.150	Percentage of all early child education	December 31, 2016	100% of emergency needs and 80% of priority needs.

No.	Project Disbursement Timing	Disbursement Type	Estimated amount		DLI	Date DLI would be measured	Information to be provided by the MOR
			%	Amount (US$M)			
					facilities with emergency needs (first number) and priority needs (second number) that received required rehabilitation (DLI 4)		
			16.667	1.150	Number of early child education professionals who received in-service training (DLI 6)	December 31, 2016	At least 1,500 professionals participated in at least 20 hours of in-service training, with documentation of participants and specific courses
			16.667	1.150	Percentage of teachers, directors, and pedagogical coordinators in fundamental education who received in-service training (DLI 7)	December 31, 2016	At least 82% of professionals participated in at least 20 hours of in-service training, with documentation of participants and specific courses
			16.667	1.150	Number of schools that received systematic follow-up on management plan from the Core Regional Follow-up team (DLI 8)	December 31, 2016	At least 120 schools received follow-up, with documentation in the form of monitoring reports and school management plans for that year for each school.
			16.665	1.150	Maintain key staff (DLI 12)	December 31, 2016	At least the deputy coordinator, a procurement specialist, a financial management specialist, and at least three focal points, with experience and functions acceptable by the Bank, have been selected, hired, and are working in the Project.
11TH DISBURSEMENT PERIOD – US$5.7 MILLION							
11	September 2017	11th reimbursement of EEP expenditures					Actual EEP expenditures incurred and paid for the period from January 1, 2017 to June 30, 2017, in a total amount not less than US$19.000 million out of

No.	Project Disbursement Timing	Disbursement Type	Estimated amount		DLI	Date DLI would be measured	Information to be provided by the MOR
			%	Amount (US$M)			
							which at least US$5.700 million shall comply with Bank's criteria and procurement rules to be considered eligible for Bank financing.
			20	1.140	Number of children enrolled in multi-sectoral ECD program (DLI 2)	June 30, 2017	At least 1,200 children enrolled, verified by enrollment records.
			20	1.140	Number of students enrolled in extended school day program (DLI 3)	June 30, 2017	At least 3,950 children enrolled, verified by enrollment records
			20	1.140	Number of students in Grades 1-5 enrolled in accelerated learning programs (DLI 5)	June 30, 2017	At least 900 students enrolled, as verified by enrollment records
			20	1.140	System for learning assessment at the primary level (SMAR) (DLI 9)	June 30, 2017	System functioning at Level 4 of utility.
			20	1.140	Maintain key staff (DLI 12)	June 30, 2017	At least the deputy coordinator, a procurement specialist, a financial management specialist, and at least three focal points, with experience and functions acceptable by the Bank, have been selected, hired, and are working in the Project.

* Effectiveness date expected to be September 3, 2012.
**Disbursement period assumes a 5-year loan. Periods are defined as six-month periods as Jan 1 – Jun 30 and Jul 1 – Dec 31, except for the first one which is from the Retroactive Financing date to the Loan Signing date and the second one which is from the Loan Signing date to December 2012.
*** The amounts are illustrative. In all cases, the value of each DLI would be calculated on the basis of the planned disbursement amount for the semester divided equally by the DLIs for the period.

Table 7: Specific Requirements and Penalties for Indicators not Met Under Component 1 of the Project

DLI	Specific Requirements and Penalties
DLI #1: Percentage of aggregate budget allocation for EEPs spent	Disbursements would be pro-rated according to the level of execution. If SEEL fails to achieve the 60 percent indicator (DLI #1), the corresponding amount to be disbursed from the loan attributable to DLI #1 would be pro-rated according to the level of execution.
DLI #2 - 8	Disbursements would be pro-rated according to the level of execution. If a DLI target is not fully achieved, an amount proportional to the extent to which the DLI was met would be disbursed. The MOR and the Bank would agree on an Action Plan to ensure the DLI target is fully achieved under the Project, and the amounts withheld for each failed DLI would be reimbursed when the DLI is achieved.
DLI #9 - 12	Disbursements would be made if the DLI is fully achieved. If a DLI target is not fully achieved, the MOR and the Bank would agree on an Action Plan and the full amount would be reimbursed once the DLI is fully achieved.
Additional requirements and penalties	Prior to the sixth disbursement (expected to take place in March 2015) the Bank and the MOR would conduct a Project MTR to evaluate, among other Project aspects, the performance of the results-based framework and the accomplishment of the Project DLIs. This MTR would determine if any new or the existing DLIs and PDIs would be required to be incorporated or modified in the current results-based framework in line with the disbursement mechanism/modalities used by the Project. If, as the result of the IVA evaluations, the MOR and/or the Bank ascertain that disbursements were made by the Bank based on data that were inaccurate or did not reflect the agreed targets, two remedies exist: (a) the disbursed amounts found not to be eligible may be deducted from the next disbursement cycle; or (b) the disbursed amounts found not to be eligible shall be returned to the Bank by the MOR. If no other disbursement cycle applies, the latter remedy would be employed.

C. Procurement

34. Procurement for the proposed Project would be carried out in accordance with the Bank's "Guidelines: Procurement under IBRD Loans and IDA Credits" dated January 2011; "Guidelines: Selection and Employment of Consultants by World Bank Borrowers" dated January 2011; and the provisions stipulated in the Legal Agreements. The various items under different expenditure categories are described in general below. For each contract to be financed by the Loan, the different procurement methods or consultant selection methods, the need for pre-qualification, estimated costs, prior review requirements, and time frame are agreed between the MOR and the Bank in the Procurement Plan. The Procurement Plan would be updated at least annually or as required to reflect the actual Project implementation needs and improvements in institutional capacity.

Procurement of goods

35. Goods procured under this Project would include school furniture; equipment; books and other learning materials; children's toys; supplies; computer and other IT equipment, ready available software and systems, etc. Procurement would be done using the World Bank's Standard Bidding Document (SBD) for all International Competitive Bidding (ICB) and National SBD agreed with or satisfactory to the World Bank for all National Competitive Bidding (NCB). Small value contracts not to exceed US$100,000 would follow Shopping procedures. Direct contracting would also be used when the conditions of paragraph 3.7 of the Guidelines are met. Under Component 1, goods contracts estimated to cost less than US$3,000,000 would follow NCB procedures. The following procedures, *convite, tomada de preços* and *concorrência*, as set forth in the Guarantor's Law No. 8,666 of June 21, 1993 as well as procurement in accordance with the method known as pregão eletrônico, as provided in the Guarantor's Law No. 10,520, of July 17, 2002, under any e-procurement system approved by the Bank, are all bidding procedures acceptable to the Bank under paragraph 3.3 of the Guidelines. Bidding documents must include anticorruption and right to audit clauses to be considered acceptable to the Bank. All contracts estimated to cost more than US$500,000 equivalent per contract and the first process, regardless of the value, would be subject to prior review by the World Bank.

Procurement of non-consulting services

36. Procurement of non-consulting services would include rehabilitation of existing schools that provide early child education (*creches*, pre-schools, and CMEIs), printing, logistics and catering services. Small value contracts not to exceed US$100,000 would follow Shopping procedures. Direct contracting would also be used when the conditions of paragraph 3.7 of the Guidelines are met. Under Component 1, non-consulting services contracts estimated to cost less than US$3,000,000 would follow NCB procedures. The following procedures convite, tomada de preços and concorrência procedures, as set forth in the Guarantor's Law No. 8,666 of June 21, 1993 as well as procurement in accordance with the method known as pregão eletrônico, as provided in the Guarantor's Law No. 10,520, of July 17, 2002, under any e-procurement system approved by the Bank, are all bidding procedures acceptable to the Bank under paragraph 3.3 of the Guidelines. Bidding documents must include anticorruption and right to audit clauses to be considered acceptable to the Bank. All contracts estimated to cost more than US$500,000 equivalent per contract and the first process, regardless of the value, would be subject to prior review by the World Bank.

Selection of consultants

37. Consulting services from firms and individuals required for the Project would include property assessment; a new tax management system including a cadastre and module for follow up of non-tax active debt; CGM's payroll management system; an in-depth diagnostic of debt management and development of a debt management system; diagnostic of human resources management in the MOR; and urban mobility management-related studies. Consultants would be selected in accordance with QCBS, CQS, QBS, LCS, SFB, SSS, or individual consultant selection procedures, as defined in the Procurement Plan. Short lists of consultants for services estimated to cost less than US$500,000 equivalent per contract may be composed entirely of national consultants in accordance with the provisions of paragraph 2.7 of the Consultant Guidelines. Under Component 1, services of consulting firms and individual consultants, estimated to cost less than US$100,000 and US$50,000 equivalent, respectively, would be procured following single/sole source selection procedures. In these specific cases, when single/sole source selection procedures may apply, the MOR might complement the review of the consultant's proposals on the basis of *técnica e preço* and/or *melhor técnica* as provided for in the Brazilian Procurement Law No. 8666, of June 21, 1993, as long as selection documents include anticorruption and right to audit clauses and the principles of economy, efficiency and equal opportunity to all qualified consultants are ensured. All contracts estimated to cost more than US$300,000 equivalent per contract and the first process under each selection method would be subject to prior review by the World Bank.

38. Operating costs: These would include equipment, rental of office space, utilities, office supplies, communication and internet costs, school's maintenance and miscellaneous expenses, and home visits. These would be procured following procedures acceptable to the Bank and outlined in the MOP.

39. The procurement procedures and SBDs to be used for each procurement method, as well as model contracts for goods to be procured are presented in the MOP, which includes detailed guidelines for implementation of the Project components, Monitoring and Evaluation, procurement, financial management, and Safeguards. All bidding documents and respective contracts, regardless of the procurement method, are required to have the anticorruption (A/C) and right to audit clause in the bidding documents and the contract as a condition for eligibility of expenditures.

Assessment of the agency's capacity to implement procurement

40. An assessment of the capacity of the participating entity to implement procurement actions was carried out in May 2011 and updated in June 2011 by the Bank's procurement team during missions for this Project. The assessment reviewed the organizational structure for implementing the Project and the interaction between the Project staff responsible for procurement (SEFIN) and the MOR. The overall Project risk for procurement is rated as Substantial. Mitigation measures for procurement implementation to be managed by the MOR have been agreed. SEFIN has no experience with processes for hiring consultants' services. At least an additional procurement specialist would be hired under the Project to strengthen the capacity of the SEFIN Procurement Unit.

Table 8: Procurement Risk Assessment and Mitigation Matrix

	Risk Assessment				**Risk Mitigation Measures**	**Residual Risk**
	H	**S**	**M**	**L**		
Project Level		X			• Provide appropriate space and furniture to the procurement staff including lockers • Train all the procurement and technical staff on Bank procurement policies • Hire a procurement specialist and sufficient support staff for each commission of bidding • Electronic system to control procurement procedures • Develop and implement a permanent training program and a certification/qualification system for procurement staff	M
Overall Rating		X				M

Note: H-High; S-Substantial; M-Moderate; L-Low

Procurement Plan

41. The procurement plan for implementation of the proposed Project was approved by the Bank on April 17, 2012. The plan would be updated annually. The recommended thresholds for the use of the procurement methods specified in the Loan Agreement are identified in Table 10.1 and 10.2 of this Annex as the basis for the agreed procurement plan. Given the nature of the

SWAp Program, the procurement plan would cover all contracts under Component 2 and only prior review goods, non-consulting services and consultancy contracts under Component 1. Supervision of procurement would be carried out through prior review supplemented by supervision missions with post review at least once a year.

Table 9: Summary Procurement Plan

Contract Type	Description of Contract	Estimated Cost (US$)	Procurement Method	Review by Bank (Prior / Post)	Estimated date of award
Component 1 – No ICB contracts have been identified up to negotiations stage.					
Component 2 –					
Consultants	Re-assessment of property values for IPTU	1,060,000	QCBS	Prior	
Consultants	Web-based revenue system	590,000	QCBS	Prior	
Consultants	Web-based tax collection system and communication campaign to facilitate the payments using bank accounts	295,000	QCBS	Prior	
Consultants	New revenue administration system	4,400,000	QCBS	Prior	
Consultants	Debt management system	590,000	QCBS	Prior	
Consultants	Strengthening of the CGM's capacity to enhance control over the MOR's payroll	590,000	QCBS	Prior	
Consultants	Payroll audit	1,200,000	QCBS	Prior	
Consultants	New payroll and human resources management system	4,700,000	QCBS	Prior	
Consultants	Modernization of procurement management	275,000	QCBS	Prior	
Consultants	Strengthening of financial and accounting management to comply with policy changes mandated at the national level (PFM)	290,000	QCBS	Prior	
Consultants	Elaboration of urban plans establishing the priority of the executive projects (mobility)	590,000	QCBS	Prior	
Consultants	Drafting of the executive projects proposed by the urban plans (mobility)	2,700,000	QCBS	Prior	
Consultants	Set up and implementation of a Unit for Monitoring the Strategic Projects	1,170,000	QCBS	Prior	
Consultants	TA to map and automate 30 key administrative procedures	1,850,000	QCBS	Prior	

Table 10.1: Thresholds for Procurement Methods and Prior Review (Component 1)

Expenditure category	Contract value threshold (US$ thousands)	Procurement method	Processes subject to prior review
Goods	≥ 3,000	ICB	All processes
	< 3,000	NCB	All processes above US$500,000
Non-consulting services	≥ 3,000	ICB	All processes
	< 3,000	NCB	All processes above US$500,000
Consulting (firms & individuals)	≥ 300	QCBS/QBS	The first process under each selection method and all processes above US$300,000
	< 300 ≥ 100	LCS/CQS/FBS	
	< 100	*Técnica e preço* and/or *melhor técnica* as provided for in the Procurement Law No. 8666 with documents acceptable to the Bank.	
Individual consultants	< 50		
Direct contracting/ Single Source Selection			All cases regardless of the amounts involved
Agreements			All cases regardless of the amounts involved

Table 10.2: Thresholds for Procurement Methods and Prior Review (Component 2)

Expenditure category	Contract value threshold (US$ thousands)	Procurement method	Processes subject to prior review
Goods	≥ 3,000	ICB	All processes
	< 3,000 ≥ 100	NCB	First process and all processes above US$500,000
	< 100	Shopping	First process.
Non-consulting serv (incl. training, communication)	≥ 3,000	ICB	All processes
	< 3,000 ≥ 100	NCB	First process and all processes above US$500,000
	< 100	Shopping	First process
Consulting (firms)	≥ 300	QCBS/QBS	All processes
	< 300 ≥ 100	LCS/CQS/FBS	First process under each selection method.
	< 100		
Individual consultants	Section V in the Guidelines		
Direct contracting and Single Source Selection			All cases regardless of the amounts involved
Agreements			All cases regardless of the amounts involved

Note: ICB = International Competitive Bidding - NCB = National Competitive Bidding
QCBS = Quality- and Cost-Based Selection - QBS = Quality-Based Selection
FBS = Fixed Budget Selection - LCS = Least-Cost Selection
CQS = Selection Based on Consultants' Qualifications

III. Environmental and Social (including safeguards)

Environmental

42. Project interventions imply some degree of rehabilitation activities, thereby triggering OP/BP 4.01 (Environmental Assessment). Most Project activities are not expected to generate adverse environmental effects. The Project involves selected rehabilitation of existing early child education centers on existing footprints. The appropriate Environmental Assessment tool is an Environmental Management Framework (EMF), which was prepared and disclosed on September 23, 2011 at www.recife.pe.gov.br and the Bank Infoshop. The EMF may be updated from time to time with the prior written agreement from the Bank. The EMF provides a description of the following: (a) the environmental mitigation and monitoring measures to be taken during implementation; (b) waste disposal measures; and (c) institutional arrangements for supervision and oversight of environmental measures. Safety measures would also ensure that students and teachers attending the schools where any construction activities are taking place are not negatively affected. As appropriate, each rehabilitation contract would specify the required environmental management measures to be followed at each site. Only rehabilitation that is on the existing building footprint would be eligible under the program, and the program therefore would not involve involuntary resettlement, social or economic displacement of persons or land acquisition

Social

43. Overall the Project is expected to have a positive social impact, via the positive social impacts of quality early child education, multidisciplinary early child stimulation, and quality fundamental education. Significant long-term evidence from around the world demonstrates benefits of early child investments across a range of social outcomes. The focus on addressing the quality of education in Recife, which has fallen behind other major municipalities in Brazil, would help to provide more equitable access to a quality education.

44. The key stakeholders in the Project include parent associations, teachers, teachers' unions, Civil Society Organizations (CSOs) involved in education delivery, taxpayers, public servants, and the municipal administration. During Project preparation no traditional indigenous communities were identified in the municipal areas where the Project would be active. The MOR has several ongoing consultative forums for involving key stakeholders in issues of education policy design and implementation. This includes the Municipal Education Conference (*Conferência Municipal de Educação*, or COMUDE), which holds periodic consultations with teachers, parent associations, educational agencies and CSOs, and which met in August 2011 to discuss the plans to improve early childhood education.

45. In addition to COMUDE, additional consultations have been held with CSOs involved in the education sector, representatives of teachers' unions, and community members in selected areas. These consultations highlighted: (a) the high level of demand for the CMEIs among both teachers and community members; (b) the importance of a holistic approach to improving early childhood education via equal focus on the quality of teaching (pedagogic content, teacher training); (c) the utility of linking Bolsa Família to access to CMEIs and to community activities held at the CMEIs; and (d) an interest among teachers in being involved in monitoring implementation of this Project, together with professionals from health and social protection.

46. Given the Project focus on improving the efficiency of education and public management, and human resource management in the MOR, some areas that will be monitored for adverse social impacts by the Project team in the course of supervision include the sensitivity of the payroll audits, the property reassessment for IPTU purposes, any potential changes to terms of work (length of work day) for teachers, and the hiring of additional teachers for expansion of the school day. Finally, as some civil servants and retirees may oppose the implementation of payroll audit findings, the Project would include financing of communications campaigns and political economy studies in order to mitigate this risk and address concerns.

IV. Monitoring and Evaluation

47. SEGESP would have primary responsibility for tracking progress related to Project outcomes and results. SEGESP would provide inputs for the sub-component on municipal planning and would coordinate inputs gathered by SEEL (education components of the Project), SEFIN (tax administration, debt management and efficiency of public expenditures), SADGP (efficiency of public expenditures), and SSP (urban mobility management). In the case of urban mobility management, information would also be prepared by the CTTU, the Greater Recife Consortium on Transport (Consórcio Grande Recife) and the Recife City Institute (Instituto da Cidade do Recife Engenheiro Pelópidas Silveira), and submitted to SSP for review and consolidation.

48. SEGESP would include the following information in each Project Report: (a) the MOR's compliance with the DLIs; (b) the updated Procurement Plan; (c) a section describing any condition which interferes or that could potentially interfere with Project implementation, including any environmental/social issues that may arise during Project implementation. The Project reports would be submitted to the Bank twice a year prior to the respective disbursement requests, but not later than 60 days after the end of the period covered by such report.

49. The MOR would, not later than eighteen months (18) months after Effectiveness date, select and contract an entity, independent from the MOR (Independent Verification Agency) with experience and qualifications in education acceptable to the Bank. The IVA would be responsible for the carrying out of at least two technical audits during the Project, particularly focused on the achievement of the DLIs.

Annex 4: Operational Risk Assessment Framework (ORAF)

Stage: Board

Project Stakeholder Risks	**Rating**	**Moderate**		
Description : The teachers' union may not support some education interventions.	**Risk Management:** The Project included consultations with the teachers' union, the Municipal Education Conference (*Conferência Municipal de Educação*, or COMUDE), community members in selected areas and CSOs involved in early childhood education during preparation. It would expand the existing Consultative Committees to include teachers in Project monitoring during implementation (emulating the strategy of the state government in implementing education reforms). The teachers' union was supportive of holistic efforts to improve the quality of early childhood education.			
	Resp: Secretariat of Education (SEEL)	**Stage:** preparation and implementation	**Due Date:** April 30, 2018	**Status:** in process
Civil Servants and retirees may oppose the implementation of payroll audit findings. Also, the re-assessment of property values for the IPTU may be considered as unpopular.	**Risk Management:** The Project would include financing of communication campaigns and political economy studies for these reforms.			
	Resp: Secretariat of Finance (SEFIN), Special Secretariat of Management and Planning (SEGESP)	**Stage:** implementation	**Due Date:** April 30, 2018	**Status:** not yet due
Implementing Agency Risks (including fiduciary)				
Capacity	**Rating:**	**High**		
Description: SEFIN, in which all municipal Bidding Committees are located, may have inadequate fiduciary capacity since it has no previous experience with Bank procurement and consultant guidelines and weak financial management capacity. It may lack proper follow up on internal and external audit reports.	**Risk Management :** During preparation, procurement and FM assessments were carried out, and generated agreed action plans. The team conducted a detailed expenditure review to map procurement characteristics of the Eligible Expenditure Programs (EEP). The Project would provide training, assistance with key terms of reference, and technical assistance on financial systems. Terms of reference would be prepared before Project effectiveness to the extent possible, and certain elements of Component 2 (such as the new payroll system) would use a significant quantity of the resources in just one procurement process. In addition, the SWAp Component allows the use for goods up to a certain threshold of national procurement rules, which are equivalent to the Bank's and well known by MOR. Furthermore, the Project is supporting the hiring of a procurement specialist to support these activities. The Project is also supporting the hiring of a financial management specialist.			
	Resp: Bank & SEFIN	**Stage:** preparation and implementation	**Due Date:** April 30, 2018	**Status:** 1st procurement training conducted in July

<table>
<tr><td></td><td></td><td></td><td></td><td>2011.</td></tr>
<tr><td rowspan="2">A potential change in Administration could result in a short-term reduction in capacity as new counterparts learn Bank processes.</td><td colspan="4">Risk Management: The Project has and would involve technical staff at each level of the MOR so that turnover after an election does not entirely eliminate capacity. The Project would have a MOP which would assist new counterparts in capacity building. In addition, five focal points will be hired in each of participating entities and can assist in a transition.</td></tr>
<tr><td>Resp: Bank and MOR</td><td>Stage: preparation and implementation</td><td>Due Date: April 30, 2018</td><td>Status: in process</td></tr>
<tr><td>Governance</td><td>Rating:</td><td colspan="3">High</td></tr>
<tr><td rowspan="4">Description :
There is a governance risk of high political interference in institutional arrangements, particularly staffing.</td><td colspan="4">Risk Management: This would be mitigated through the selection and hiring of a technical coordinator (deputy coordinator), with terms of reference and qualifications acceptable to the Bank, and creation of a Consultative Committee with structure and functions defined in the MOP that can help strengthen staff.</td></tr>
<tr><td>Resp: SEGESP</td><td>Stage: implementation</td><td>Due Date: not later than two (2) months after Effective Date</td><td>Status: not yet due</td></tr>
<tr><td colspan="4">Risk Management: The Project would improve the audit and payroll systems and would observe Bank anti-corruption measures. The technical assistance component of this Project would work with the MOR to address the risk of financial mismanagement.</td></tr>
<tr><td>Resp: All participating entities</td><td>Stage: implementation</td><td>Due Date: April 30, 2018</td><td>Status: not yet due</td></tr>
<tr><td>Project Risks</td><td colspan="4"></td></tr>
<tr><td>Design</td><td>Rating:</td><td colspan="3">Substantial</td></tr>
<tr><td rowspan="2">Description :
A design risk is posed from the potential difficulty in identifying sufficient eligible expenditures to be financed by the Bank under the EEPs (Component 1).</td><td colspan="4">Risk Management: This risk has been mitigated during preparation by a detailed review of the following activities: (i) the composition of expenditures of SEEL’s budget; (ii) SEEL’s budget execution in years 2010 and part of 2011; and (iii) a list of at least 60 ongoing contracts, non procurable items, and recurrent expenditures to find potential expenditures to be retroactively financed. Programs to be co-financed were identified that have been successfully disbursed and presented lower procurement risk in 2010 and the first semester of 2011. During preparation, the MOR prepared and published Law 17.765, dated January 5, 2012, to allow the use of Bank procurement rules before Loan signature. However, this risk may persist during implementation given uncertainties related to budget execution, which are inherent to the public administration process.</td></tr>
<tr><td>Resp: Bank, SEEL, and SEGESP</td><td>Stage: preparation and implementation</td><td>Due Date: April 30, 2018</td><td>Status: in process</td></tr>
<tr><td rowspan="2">The Project includes new programs such as the late-grade accelerated learning program and the expansion of the school day, which can require design revisions, leading to the risk of delays.</td><td colspan="4">Risk Management: This design risk has been mitigated through selection of programs for which there is extensive experience at the State level and elsewhere in Brazil, so that there is consensus on appropriate design.</td></tr>
<tr><td>Resp: SEEL, Bank</td><td>Stage: implementation</td><td>Due Date: April 30, 2018</td><td>Status: not yet due</td></tr>
</table>

Mayoral elections at the end of 2012 could lead to a change in the Administration and interest in changing, given different priorities, the choice and scope of programs or technical assistance activities under the Project.	**Risk Management:** This risk is being mitigated by: (i) focusing, in Component 1, on activities which are a federal mandate (expanding ECE coverage); (ii) selecting activities with broad, non-partisan priority and consensus (improving conditions for learning, eliminating payroll irregularities); and (iii) including DLIs associated to the needed studies and implementation of reforms			
	Resp: Bank, SEGESP, SEFIN, SADGP.	**Stage:** preparation and implementation	**Due Date:** April 30, 2018	**Status:** in process
Social and Environmental	**Rating:**	**Moderate**		
Existing early child education center rehabilitation could have adverse environmental impacts.	**Risk Management:** An Environmental Management Framework has been prepared by the MOR that provides a framework for mitigating environmental impacts.			
	Resp: SEEL, Recife Urbanization Company (*Empresa de Urbanização do Recife* – URB), SEGESP	**Stage:** preparation and implementation	**Due Date:** April 30, 2018	**Status:** in process
Program and Donor	**Rating:**	**Low**		
Description : No issues identified	**Risk Management :**			
	Resp:	**Stage:**	**Due Date :**	**Status:**
Delivery Monitoring & Sustainability	**Rating:**	**Moderate**		
Description: The SEEL and other participating entities may have difficulties in monitoring Project indicators, including the DLIs	**Risk Management:** This risk is being mitigated by selecting measurable indicators, detailing protocols, and using institutional sources readily available and with a good reputation. An IVA would also be financed by the Project to confirm twice during Project life the quality and accuracy of information.			
	Resp: Bank and MOR	**Stage:** preparation and implementation	**Due Date:** April 30, 2018	**Status:** in process
Overall Risk Following Review				
Implementation Risk Rating: High				
Comments: The overall implementation risk is considered high, largely driven by the possible change in priorities due to municipal elections and possible transition costs, including limited previous experience with Bank processes in procurement.				

Annex 5: Implementation Support Plan

Strategy and Approach for Implementation Support

1. The Implementation Support Plan (ISP) for the Project is based on the following facts: (a) the Project would not involve substantial decentralization of funds – most activities to be supported under the EEPs by Component 1 are to be conducted by SEEL and procured through the Bidding Committee at SEFIN; (b) a financial management assessment and a procurement assessment were carried out and identified the risks, expected bottlenecks for Project implementation, mitigation measures and levels of reviews and supervision; (c) the team conducted dialogue with SEEL and other participating entities on the reforms needed, and provided opportunities to discuss with other state and municipal secretariats in Brazil, and other and technical experts; (d) consultations with beneficiaries were conducted under the social safeguards umbrella; (e) budgetary analysis and other operational and procurement activities were conducted to mitigate risks associated with the SWAp approach; and (f) the MOR and the World Bank team extensively discussed and agreed on Project disbursement arrangements, including expected schedule and amounts, as well as additional instructions and penalties, especially for disbursements under Component 1, based not only on eligible expenditures, but on the achievement of DLIs.

Implementation Support Plan

2. The ISP would focus on the following areas and activities:

- Technical inputs needed: (a) technical professionals and experts to support the elaboration of TORs in all participating entities, and technical focal points in the five participating entities; (b) field visits to other experiences in Brazil (and abroad) in the areas of education and public management to learn innovative and successful practices; (c) creation of the Consultive Committee to support Project implementation by each participating entity; (d) creation of the PIU with key staff to support Project implementation and cross support to participating entities; (e) inclusion of technical and fiduciary covenants, and a DLI to ensure presence of key staff for Project management during implementation; and (f) hiring of IVA.

- Fiduciary requirements and inputs: (a) put in place a PIU with operational and fiduciary staff, with qualifications acceptable to the Bank; (b) support modernization of the Bidding Committees located at SEFIN, including physical structure; (c) support adoption of *pregão eletronico* by the municipal Bidding Committee; and (d) provide training.

The Project includes the following elements of implementation support for the first two years:

Time	*Focus*	*Skills Needed*	*Resource Estimate*	*Partner Role*
First twelve months	Hiring of PIU staff	Deputy coordinator (project management skills); Procurement specialist; Financial management	US$300,000	Not applicable

		specialist; at least three focal points (management and technical skills)		
	Establishment of the Consultative Committee		US$5,000	
	Fiduciary training (twice a year)		US$20,000	
	Acquisition of equipment and systems		US$100,000	
12-48 months	Keep PIU staff	Same as above, as well as other skills as identified		
	Maintain Consultative Committee		US$5,000	
	Hire IVA		US$50,000	
	Field visits		US$30,000	

In addition to the supplementary needs above, the Project will require the following supervision in the first two years:

Skills Needed	***Number of Staff Weeks***	***Number of Trips***	***Comments***
Operations specialist (Co-TTL)	12	4	Operations specialist will oversee the whole operation and sub-component 2(g).
Education specialist (Co-TTL)	12	4	Education specialist will oversee whole operation and supervise all of Component 1 and sub-component 2(a).
Public Sector specialist	10	4	Public sector specialist will supervise sub-components 2(b) through 2(e).
Urban mobility specialist	10	4	Urban mobility specialist will supervise sub-component 2(f).
Procurement specialist	12	4	Procurement specialist will support the MOR on related issues.
Financial management specialist	10	4	FM specialist will support the MOR on related issues.
Disbursement specialist	5	2	Disbursement specialist will support MOR on disbursements.

Annex 6: Economic and Financial Analysis

A. Economic Analysis

1. As described in the context section of this document, the MOR of Recife's (Município do Recife – MOR) education and public management system faces many problems. Recife's students consistently perform poorly on national tests, age-grade distortion is high, teacher quality is lacking, and time for instruction is limited. This Project seeks to address several of these challenges.

2. The Project would expand coverage of improved ECE, create conditions more conducive to learning in fundamental education, and improve municipal public management. The best evidence on returns to investments in early child education comes from randomized trials in the United States, such as the Perry Preschool Program, which yielded a return of 7 to 10 percent.[18] These returns come through a range of channels, from improved incomes associated with higher education to reduced criminality and reliance on welfare programs. A study in northeastern and southeastern Brazil showed higher returns of 12.5 to 15 percent to early child education, with an additional 0.5 years of total schooling for ECE participants and – for men – a 2 to 6 percent earnings increase, with even higher returns for the poor.[19] (However, this second study has more potential to be subject to selection bias in its analysis.) Evidence from six state capitals around Brazil shows that quality is essential to obtaining returns to early child education; low quality centers delivered the same returns as not participating in early child education.

3. An alternative to the standard expansion of centers is home-based early child stimulation. This may yield similar benefits to center-based stimulation but without the fixed costs of constructing centers (and also without providing child care to mothers). However, home-based visits are associated with very high recurrent costs, as employees must travel to children's homes. The relative return between these two alternatives is unknown; as such, the MOR is expanding the type of care with which it has most experience – center-based care – and implementing a smaller-scope pilot program of a multi-sectoral home-based program.

4. The scope of the multi-sectoral home-based program is small, as it is a pilot. It would reach 1,400 children age 0-3, which is a tiny fraction of the 77,365 children of that age group in the MOR. However, the pilot would be implemented in just one area – Region 4 – and should cover the 20 percent of children most vulnerable within that region. The costs are high as they include initial design of the program as well as piloting. The rate of return is challenging to estimate, as there are only two similar programs in Brazil, neither of which has a completed rigorous evaluation. *Primeira Infância Melhor*, based in Rio Grande do Sul, has demonstrated gains in cognitive, social, and motor development in participating children relative to similar children in the same communities.

5. The Project would support rehabilitation of all 75 existing public early child education centers in Recife. This should reach 34 percent of children currently enrolled in ECE in the

[18] Heckman JJ et al, "The Rate of Return to the High/Scope Perry Preschool Program," Journal of Public Economics 2010.

[19] Young ME, "Brazil Early Child Development: A Focus on the Impact of Preschools," World Bank Report No. 22841-BR, 2001.

MOR, particularly the most vulnerable, as these are much more likely to access public ECE. Recent evidence from six capitals around Brazil demonstrates that higher quality ECE centers result in two percent higher test scores. A study in Rio de Janeiro demonstrates that improved physical infrastructure specifically has significant impacts on both social (3.8 months of child development) and physical (2.4 months) development.

6. The Project would improve education through the expansion of the school day for the most struggling fundamental education students. The program would annually attend 1,557 students in the third year of fundamental education and 1,690 students in the fifth year of fundamental education. The total number of students in fundamental education in Recife is 74,000, but the SEEL has identified 7,789 struggling students in the third year and 8,452 struggling students in the fifth year, so the program should reach 20 percent of struggling students each year. Evidence from expansion of the school day in Chile shows positive impacts on a range of outcomes, including academic outcomes, cognitive and socio-economic test scores, reduction of adolescent motherhood and high school dropout.[20] In Argentina, a similar expansion showed major improvements (21 percent) in high school graduation rates, which are associated with significant increases in earnings.[21]

7. The Project would support accelerated learning programs in the early years of fundamental education, reaching 6,518 students in early years over the course of the Project. This is expected to yield benefits in terms of quicker progression through school (and thereby quicker entry into the job market) and children leaving school with more years of learning.

8. The MOR would implement a student evaluation program to supplement the state evaluation. This would benefit all students in public education in the MOR, and would allow – for the first time – value-added evaluation of students year by year. Because the municipal evaluation system would test those years not tested by the state system, the MOR would have test score data for students in each year of their progress through the education system, allowing much more careful analysis of teacher and school value added over time.

9. Public management reforms, including tax administration reform, public debt management, payroll management, results-based management, and urban mobility management are expected to benefit citizens on a broad scope. Tax administration reforms are expected to increase tax revenues by 20 percent over the course of the Project simply by updating the property values. Likewise, payroll audits are expected to result in at least R$7.2 million yearly savings in payroll expenditures by reducing irregularities. Results-based management, public debt management, and urban mobility management yield more quality improvements that permit the entire municipal system to function more effectively.

[20] Pires T and Urzua S, "Longer School Days, Better Outcomes?" working paper, 2010.
[21] Llach J, Adrogué C, and Gigaglia M, "Do Longer School Days Have Enduring Educational, Occupational, or Income Effects? A Natural Experiment in Buenos Aires, Argentina," Economia, 2009.

B. Fiscal Situation 2003-2010

B.1. Basic Fiscal Figures

10. After years of fiscal deterioration, Recife's municipal government had some improvement in its financial performance. A Bank fiscal analysis for the *Capibaribe Melhor* project (P089013) covering the period 1999-2003 had showed a significant deterioration in the fiscal situation, which continued in the initial years of the period covered by the present analysis – 2003-10[22]. If we don't consider those extraordinary revenues, primary balance would turn into a 6.2 percent NCR deficit in 2004, would be close to zero in 2005 and deficit would reach 4.8 percent NCR in 2007. That means that in 5 out of the 8 years 2003-10 period the MOR would have no coverage even for interest payments. The years 2009 and 2010 show an improvement in the fiscal situation, recovering a positive primary balance and also fiscal year surpluses. Nevertheless, we should take into account that 2009 was a first year administration, when expenses are naturally lower than in the previous year. To understand those movements, some important aspects must be pointed out. Table 1 sets forth the basic fiscal figures for the period.[23]

11. This analysis counts on data taken from financial reports available at the Ministry of Finances and at the Recife Municipal sites, complemented by information supplied by the MOR. We should point out that the last report of the Court of Accounts dates from 2004. Additional information about state transfers was collected from the State Government of Pernambuco site. Comparisons to other cities utilized among others data from the Central Bank, from the Federal Bureau of Statistics – IBGE and from the state research institute – CONDEPE FIDEM.

[22] In the period, two different teams managed the municipal government: 1999 was the third year of Mayor Roberto Magalhães. In 2001, Mayor João Paulo took office and was reelected for another four year term- 2005 to 2008. In 2009, Mayor João da Costa, same party as previous Mayor – Labour Party – took office.

[23]All the information on revenues, expenditures and debt is adjusted for inflation to the price levels of 2010, through the IIPCA/IBGE. Variations in figures are therefore real.

Table 1: Municipality of Recife Fiscal Balances – 2003-10

R$ million 2010*

	2003	2004	2005	2006	2007	2008	2009	2010
I. REVENUE	**1,480.2**	**1,789.4**	**1,833.2**	**1,972.8**	**2,079.9**	**2,255.6**	**2,322.9**	**2,357.5**
Taxes	529.6	557.1	600.9	643.6	694.1	733.9	749.1	814.0
Social Contributions	4.7	3.7	6.1	43.6	53.2	64.8	79.5	83.9
Intergovernmental Transfers	838.0	905.4	991.1	1,057.5	1,092.8	1,282.8	1,325.5	1,303.5
Other Revenues	107.8	323.2	235.0	228.2	239.8	174.1	168.8	156.1
of which: interest on cash available	36.4	28.1	51.7	66.0	52.7	45.0	47.3	37.0
II. EXPENSE	**1,433.2**	**1,595.6**	**1,574.1**	**1,764.4**	**1,910.1**	**2,021.5**	**2,008.4**	**2,106.4**
Compensation of Employees	563.2	614.7	635.9	688.0	758.5	832.4	849.7	944.5
Pensions	122.8	126.4	129.7	144.8	151.5	164.9	176.6	199.2
Goods and services	733.2	843.5	798.7	920.1	988.5	1,013.9	972.1	954.5
Interest Payments	14.0	10.9	9.8	11.5	11.7	10.2	10.1	8.3
III. GROSS OPERATING BALANCE	**47.0**	**193.8**	**259.1**	**208.4**	**169.7**	**234.1**	**314.5**	**251.1**
IV. TRANSACTIONS IN NON FINANCIAL ASSETS – net acquisition	**83.3**	**105.4**	**79.2**	**121.1**	**171.2**	**210.2**	**159.4**	**167.5**
Investments***	83.3	105.4	79.5	121.1	171.7	211.0	159.4	167.5
Sale of Non Fin. Assets	(0.0)	0.0	(0.3)	0.0	(0.5)	(0.8)	0.0	0.0
V. NET LENDING/BORROWING**	**(36.3)**	**88.4**	**179.8**	**87.3**	**(1.5)**	**23.9**	**155.1**	**83.5**
VI.TRANSACTIONS IN FINANCIAL ASSETS -net acquisition	**0.9**	**0.0**	**0.2**	**1.9**	**0.7**	**(0.0)**	**0.2**	**2.2**
Constitution/Increase of capital of owned Public Companies	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other Acquisition net	0.9	0.0	0.2	1.9	0.7	(0.0)	0.2	2.2
Sale of Non Fin. Assets	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
VII. NET INCURRENCE OF LIABILITIES***	**37.2**	**(88.4)**	**(179.7)**	**(85.4)**	**2.2**	**(23.9)**	**(154.9)**	**(81.3)**
Debt Amortizations	(21.0)	(19.7)	(24.6)	(26.6)	(30.2)	(37.8)	(53.7)	(47.1)
New Loans	0.0	0.0	1.6	43.4	11.8	2.4	6.7	23.5
Fiscal Year Deficit****	58.2	(68.8)	(156.7)	(102.2)	20.7	11.4	(108.0)	(57.7)
NET CURRENT REVENUE – NCR	**1,461.7**	**1,767.5**	**1,808.2**	**1,920.9**	**1,989.0**	**2,118.1**	**2,184.8**	**2,248.3**
PRIMARY BALANCE	**(59.6)**	**71.3**	**137.5**	**30.5**	**(43.9)**	**(11.9)**	**117.6**	**52.5**
PRIMARY BALANCE/NCR%	**(4.1)**	**4.0**	**7.6**	**1.6**	**(2.2)**	**(0.6)**	**5.4**	**2.3**

Source: Financial Statements of the MOR
*Figures adjusted by the Consumer Price Index -IPCA/IBGE
**Net lending:(+) for lending (-)for borrowing
***Net incurr. Liabilities (+)for increase of liability;(-)for decrease
****Fiscal Year Result(+) for deficit (-) for surplus

12. In the period 2003-10, revenue grew at an average yearly rate of 6.9 percent due mainly to the increase of the Tax on Services – ISS (7.9 percent), but also to the transfers from the Fund of Participation of Municipalities – FPM (7.8 percent) and from the Unified Health System – SUS (9.2 percent). Although a less significant amount, the better performance relates to the collection of social contributions from public employees, almost inexistent by 2003 and now accounting for almost 40 percent of Pensions payments. The resources are assigned to the payment pensions - retirees and survivors. The pension fund – RECIPREV was created by law in 2001, but began to operate only in 2005. In 2010, the dependency ratio – the ratio of beneficiaries to active workers) was 38 percent, relatively low. Nevertheless, deficiencies in payroll data system hamper the

administration of the pension system. Inconsistency of information about employees makes difficult the assessment of pension liabilities.

Table 2 shows the breakdown of revenues.

Table 2: Municipality of Recife – Revenue Composition 2003-10

R$ million 2010*

	2003	2004	2005	2006	2007	2008	2009	2010
TOTAL REVENUE	**1,480.2**	**1,789.4**	**1,833.2**	**1,972.8**	**2,079.9**	**2,255.6**	**2,322.9**	**2,357.5**
I.MUNICIPAL TAX REVENUE	**529.6**	**557.1**	**600.9**	**643.6**	**694.1**	**733.9**	**749.1**	**814.0**
Urban Land and Property Tax – IPTU	132.9	141.7	150.5	160.4	170.1	175.6	180.1	185.2
Tax on Services – ISS	238.7	269.0	294.9	317.9	334.7	345.0	366.1	407.0
Income Tax Withheld at Source – IRRF	27.5	31.1	31.0	36.8	41.0	47.6	45.3	56.0
Other	130.5	115.3	124.5	128.4	148.4	165.6	157.7	165.8
II. PENSION FUND CONTRIBUTIONS	**4.7**	**3.7**	**6.1**	**43.6**	**53.2**	**64.8**	**79.5**	**83.9**
III. OTHER REVENUES	**107.8**	**323.2**	**235.0**	**228.2**	**239.8**	**174.1**	**168.8**	**156.1**
Economic Contributions	0.0	30.0	36.2	48.9	51.3	50.8	50.6	49.8
Interest On Cash Available	36.4	28.1	51.7	66.0	52.7	45.0	47.3	37.0
Miscellaneous	71.5	265.1	147.1	113.3	135.7	78.2	70.9	69.3
IV. INTERGOVERNMENTAL TRANSFERS	**838.0**	**905.4**	**991.1**	**1,057.5**	**1,092.8**	**1,282.8**	**1,325.5**	**1,303.5**
Municipalities Participation Fund – FPM	181.6	182.0	213.3	201.4	221.5	328.4	299.5	307.5
Unified Health System -SUS	133.7	158.6	161.2	193.2	167.5	178.6	233.3	247.2
Participation in the ICMS	423.6	437.6	479.5	524.1	539.1	573.6	593.9	589.6
Education- FUNDEF/FUNDEB	0.0	0.0	(3.0)	(4.5)	(17.9)	(30.7)	(34.2)	(43.1)
Transfers from FUNDEF/FUNDEB	0.0	0.0	27.9	105.1	117.1	145.0	163.6	156.7
Contributions to FUNDEF/FUNDEB	0.0	0.0	(30.9)	(109.6)	(134.9)	(175.8)	(197.8)	(199.7)
Other Current Transfers	85.3	108.9	121.3	134.9	144.9	160.4	174.4	176.9
Capital Transfers	13.8	18.3	18.8	8.3	37.7	72.6	58.6	25.3

Source: Financial Statements of the City of Recife
* Figures adjusted by the Consumer Price Index -IPCA/IBGE

13. Recife has a high relation of tax revenues to intergovernmental transfers – 62 percent, close to the average rate for Brazilian municipalities with population higher than 500 thousand people. In the period, while tax revenue had a more stable path, transfers grew irregularly.

14. On the tax revenue side, we should point out the weak performance of the Property Tax. It should be considered that the IPTU has been losing position among municipal tax revenues not only in Recife but in Brazil. In 2003, it represented 30.4 percent of total municipal tax revenues, sliding to 24.2 percent in 2008, while the Tax on Services increased from 35.8 percent to 44.4 percent. In the case of Recife, reasons can be found on lack of initiatives on tax management and perhaps on political matters. The last revision of property registers occurred in 1997 and covered only 60 percent of the properties. On the political side, besides the common high sensibility of the population to changes on IPTU legislation, the updating of land and property values has to be approved by the Municipal Council (same rule for all the municipalities).

15. As it happens to big cities in Brazil (and all over the world), services is a major and fast growing economic activity. In Recife, services accounted for 82.5 percent of GDP in 2008. Tax collection of ISS is concentrated on civil construction, financial services, health and technical consultancy, which were responsible for more than 42 percent of total collection in 2010. The ISS

tax management has been modernized, with the adoption of the electronic fiscal note system, but coverage is still limited to major taxpayers. This may have helped to increase tax collection even during the global crises in 2009[24.] According to the officer responsible for tax collection, there's a constant monitoring of major tax payers. Nevertheless, it seems no report is regularly produced on any municipal tax.

16. Let's now turn to intergovernmental transfers, where the FPM had an excellent performance, due to the federal Income Tax and to the Tax on Industrialized Products, which collection is shared with municipalities (23.5). In 2009, the SUS provided a substantial amount of resources to municipalities (and to the states) due mainly to a revision of the per capita values that partially regulate the amounts transferred. The worst performance was played by the ICMS, due to the loss of economic position of Recife in the State of Pernambuco.[25] Indeed, Recife's GDP accounted for an average 33 percent of state GDP in 2003-2007, falling to 31.9 percent in 2008 (last information available). The share of the MOR in the distribution of the (25 percent) of ICMS fell constantly from 36.45 percent in 2004 to 33.45 percent in 2009, and 27.60 percent in 2011. The final result was mitigated by the sound performance of the state, which tax collection grew at an average year rate of 9 percent.

17. In 1996, a Constitutional Amendment (no.14/96) instituted an intergovernmental financial cooperation for improving elementary education. The fund is formed by earmarking percentages of transfers from the revenue sharing system so as to guarantee a specified minimum amount of spending per student enrolled in public schools all over the country (except university education). The sources of the initial FUNDEF, transformed in 2007 in the FUNDEB, to cover not only the fundamental education, but also the other services rendered by states and municipalities, were expanded.[26]

18. As soon as the Fund was instituted, the Municipal government went to court and got an injunction to stop contributing to FUNDEF. As the responsibility of the State of Pernambuco in fundamental education was (and still is) relatively high, the MOR refused to participate. Court decision required the MOR to participate in Funs redistribution. Since 2005, municipal recovery of resource from the Fund has been decreasing to an average rate of 80 percent. That means that part of the resources assigned to education by the MOR – 25 percent of own tax revenues and constitutional transfers - finances other municipal school nets (the State also has a negative balance on return x contributions to the Fund. The MOR does not have an estimate of the amounts it can be required to pay relating to the period 1999-2004. According to municipal officers, past contributions have not been required up to the moment.

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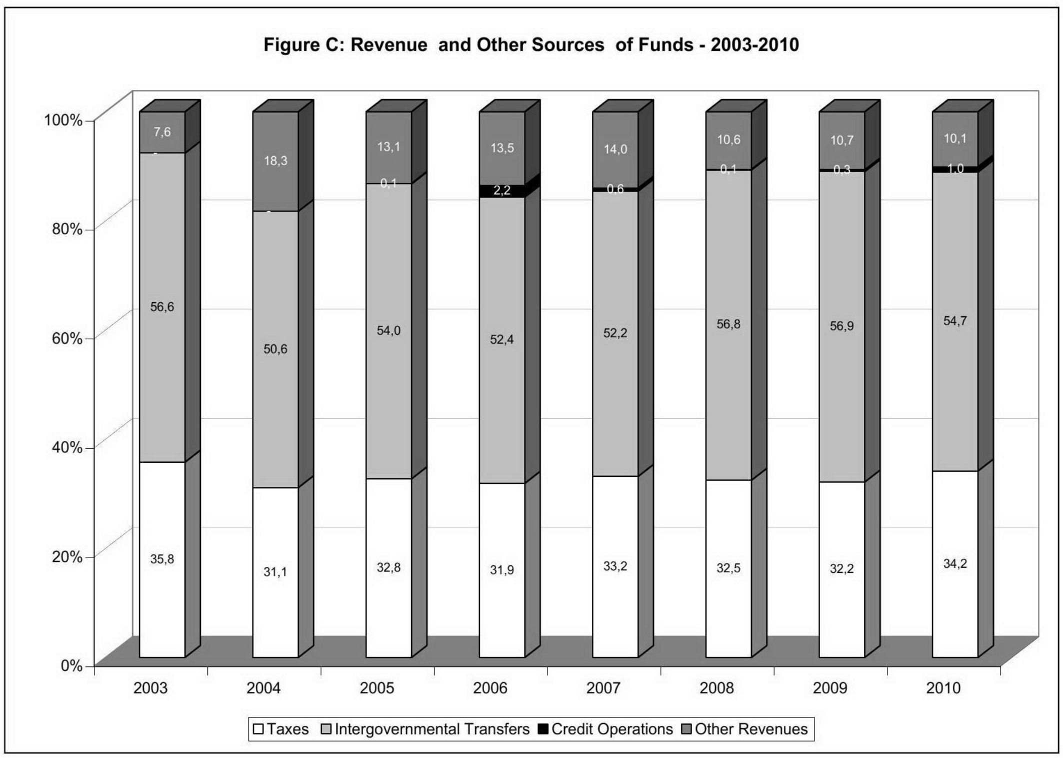
[24]Total municipal collection of ISS had a slight real decrease in 2009, although improving its participation in total taxes collected by the three levels of government – the federal government, the states and the municipalities. ISS accounted for 2.07% of total collection in 2008 and 2.12% in 2009, reaching 0.71% of GDP.

[25]25% of the State ICMS collection is shared among each state's municipalities according to the value added through operations in their territories (75% of the amount to be shared) and to a State Law (25% of amount shared, generally in benefit of the poorest). From this transfer, 20% is credited to the Fund for Education - FUNDEF/FUNDEB and the remaining 80% directly to the municipalities.

[26]Presently the **major** revenues on which states and municipalities have to contribute are: a) 20% of the municipal and states share in the ICMS; b) 20% of the FPM and FPE (states) c) 20% of the IPVA, a motor vehicles states tax . FUNDEB is distributed according to the number of students enrolled in municipal or state owned schools. Early childhood education (in day care centers is also include. In the states where the money collected from these sources is not enough to guarantee the legal minimum spending established by the federal government (generally the poorest states), the Federal Treasury provides supplementary transfers.

19. As previously pointed out, the Municipal government relied deeply on extraordinary revenues – accounted for as other revenues - from 2004 to 2007. In 2004, gross operating balance would have been close to zero if the MOR had not succeeded in passing a bill to recover resources previously transferred to the Pension Fund – R$ 181.0mm. According to the MOR, those resources should return to the Municipal Treasury since the social benefits had been fully paid by the Treasury. In 2005-7, the MOR counted again on extraordinary revenues: another R$57.0mm came from the Pension Fund in 2005. In 2006-7, a negotiation with commercial banks related to the municipal bank accounts and payroll payment resulted in extraordinary revenue – R$ 30.0mm in 2006 and R$52.0mm in 2007 (all at 2010 prices).

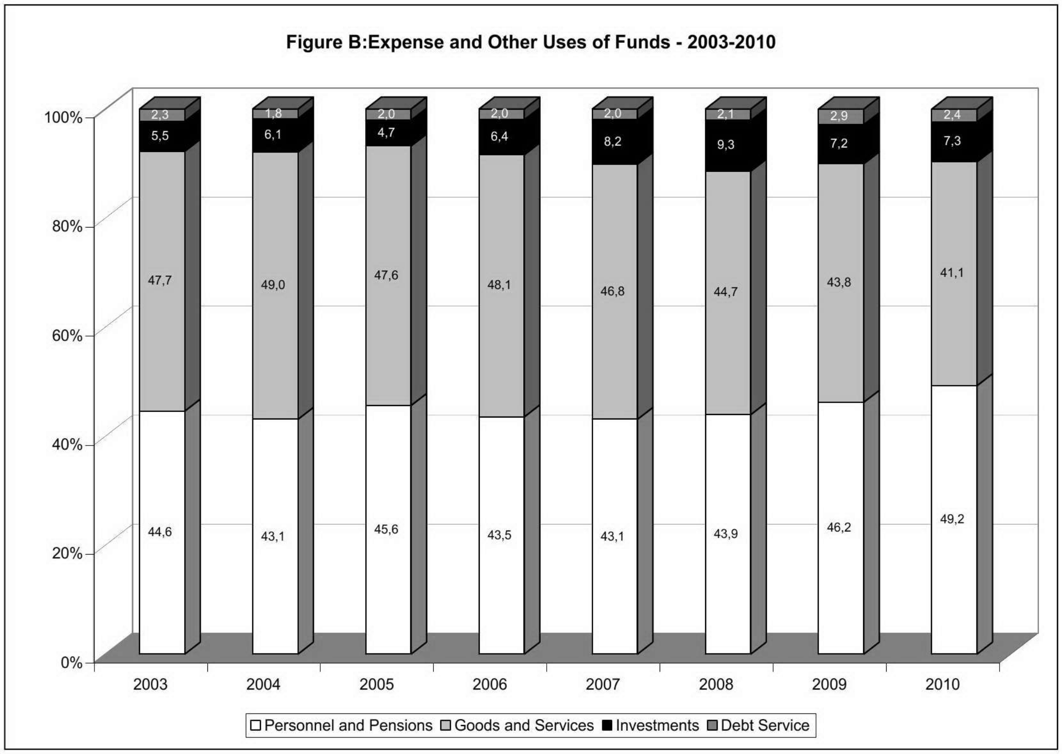
20. The situation was kept under control, since personnel expenses were stable and even reduced, related to Net Current Revenue – NCR to average 41 percent NCR in 2004-7 and debt service was low. Figure 1 shows the evolution of the composition of municipal resources along 2003-10.



21. As in most of the cities in Brazil, investment had to be financed by current account savings and/or by intergovernmental transfers, as the access to credit operations was drastically reduced, as part of the overall adjustment of the Brazilian public sector. Since 2007, the level of investment has been fluctuating around 7 percent of NCR, very low if compared to the average 9.5 percent of municipalities over 500 thousand people.

22. The recent pattern followed by the components of expenses deserve attention. Personnel expenditures climbed fast – more than 11.5 percent over inflation in 2010. It is worth noting that the number of active public servants increased by only 2 percent and retirees/ survivors by around 3.5 percent. On the other side, since 2008, goods and services have been reduced, although

transfers for health – SUS – has increased[27], what signals a strong reduction in expenses in other areas. We don1t have information about costs, to evaluate if the reduction results in less services provided to the population. Figure 2 shows the evolution of the composition of municipal resources along 2003-10.



23. Taking into consideration the overall movement in the period, we see that the Municipal government maintained a relatively low level of investment, following its reduced capacity to finance it. In fact, the external sources – capital transfers and credit operations – were disappointingly low, with a slight increase in 2008-2010. This undermines the capacity of the Municipal government to develop long term projects, since they usually require matching municipal revenue to credit operation and to capital transfers, as long as the projects develop.

24. Facing a more rigid expenditure structure, given the increasing participation of earmarked revenue as SUS, the government must control the increase of personnel expenses, which already reached the average ratio to NCR for municipalities of over 500 thousand people.

B.2. Consolidated Debt and Debt Capacity

25. Consolidated debt increased considerably during the period, as shown in Table 3. The decrease in the bank debt (half of which with the National Treasury in 2010) was more than offset by rescheduling of debts related to Social Contributions in arrears of the indirect administration that now account for 85 percent of gross debt.

[27]Resources from SUS are generally assigned to the maintenance of the municipal health net as well as to the payments of private health units that render free services to the population. This happens because Recife is entitled to operate the "Gestão Plena" in its territory, what mans that it coordinates services rendering by municipal and by private units under agreement with the Ministry of Health.

Table 3: Municipality of Recife – Consolidated Debt 2003-10

in R$ million 2010*

	2003	2004	2005	2006	2007	2008	2009	2010
CONSOLIDATED DEBT- CD (I)	**566.6**	**723.6**	**767.8**	**806.8**	**998.0**	**877.0**	**855.9**	**851.9**
Bank Loans - Direct Administration	210.9	182.9	160.2	186.9	189.0	163.2	136.1	131.7
Debt Rescheduling Taxes and Social Contributions Direct and indirect Administration	350.6	340.7	226.0	214.9	231.5	713.1	719.2	720.2
Other Debts	5.2	200.1	381.6	405.0	577.5	0.7	0.6	-
DEDUCTIONS (II)	**298.9**	**228.4**	**273.4**	**382.7**	**370.6**	**285.4**	**320.0**	**318.4**
Financial Assets	329.9	257.2	319.6	447.0	418.6	344.8	380.0	368.1
Processed Floating Debt	31.0	28.8	46.2	64.3	48.0	59.4	60.0	49.7
NET CONSOLIDATED DEBT	**267.7**	**495.3**	**494.3**	**424.0**	**627.4**	**591.6**	**535.9**	**533.5**
NET CURRENT REVENUE	**1,461.7**	**1,767.5**	**1,808.2**	**1,920.9**	**1,989.0**	**2,118.1**	**2,184.8**	**2,248.3**
CONSOLIDATED DEBT/NCR %	**38.8**	**40.9**	**42.5**	**42.0**	**50.2**	**41.4**	**39.2**	**37.9**
NET CONSOLIDATED DDEBT / NCR(%)	**18.3**	**28.0**	**27.3**	**22.1**	**31.5**	**27.9**	**24.5**	**23.7**
FEDERAL SENATE DEBT LIMIT <120%*RCL	**1,754**	**2,121**	**2,170**	**2,305**	**2,387**	**2,542**	**2,622**	**2,698**

Source: Financial Statements of the Municipality of Recife
*Figures adjusted by the Consummer Price Index -IPCA/IBGE

26. The decrease in bank debt (half of which with the National Treasury in 2010) was more than offset by rescheduling of debts related to Social Contributions in arrears of the indirect administration. Debt with the National Treasury relates mostly to renegotiations until 1994. Debt with banks decreased, as credit operations were not significant. Other debts 2007 refers to social contributions which along the renegotiation process.

27. Control of MOR's debt is highly deficient. The Secretariat of Finance doesn't record indirect administration bank debt. We may suppose it is not significant or even is inexistent[28], since there were not guarantees registered by Municipal Treasury along 2003-2010.On the other side, even after 2001/03, when the Social Security National Institute – INSS made a statement of debts in arrears and the MOR began to renegotiate, any controls were set to avoid new liabilities.

28. Deficiency is not limited to outstanding debt control. The initial conditions of INSS renegotiated debts were changed by new rules for all the Municipalities set by Law 11,960/2009, including a new methodology to calculate monthly installments. The INSS informed the MOR that the payments since then are lower than the amount due according to new rules but apparently no initiative was taken to make clear the correct amount. As is clear, lack of control is not restricted to indirect debt, but also to direct administration. Urgent initiatives are needed to avoid accumulating new liabilities.

B.3. Fiscal Responsibility Law Compliance

29. Table 4 sets forth the ceilings required by the FRL regarding debt and personnel. In the period, debt indicators were low, as most of Brazilian municipalities. Nevertheless, we should point out that, among the capital cities that renegotiated debts with the federal government, Recife's outstanding debt accounted for 11 percent of the total (excluding Rio de Janeiro and São

[28]Municipal Indirect Administration includes Foundations, Autarchies and Public Companies, whose level of indebtedness is generally low. Indirect Administration loans are generally guaranteed by Municipal Treasury.

Paulo). Personnel expenses, that were kept stable as a percentage of NCR in 2004-2007, rose sharply in 2010, as a result of average salary increases (the number of public servants was almost the same as in 2009).

Table 4: Municipality of Recife – Compliance with Fiscal Responsibility Law Limits 2003-10

R$ million 2010*

	Legal Ceiling %NCR	2003	2004	2005	2006	2007	2008	2009	2010
Net Current Revenue – NCR		**1,461.7**	**1,767.5**	**1,808.2**	**1,920.9**	**1,989.0**	**2,118.1**	**2,184.8**	**2,248.3**
Credit Operations		**-**	**-**	**1.6**	**43.4**	**11.8**	**2.4**	**6.7**	**23.5**
% NCR	≤16%	-	-	0.1	2.3	0.6	0.1	0.3	1.0
Net consolidated Debt		**267.7**	**495.4**	**498.5**	**424.0**	**627.4**	**591.6**	**535.9**	**533.5**
% NCR	≤120%	18.3	28.0	27.6	22.1	31.5	27.9	24.5	23.7
Debt Service		**35.0**	**30.6**	**34.4**	**38.1**	**41.9**	**48.0**	**63.7**	**55.4**
% NCR	≤11,5%	2.4	1.7	1.9	2.0	2.1	2.3	2.9	2.5
Net Personnel expenses		**679.9**	**723.1**	**754.5**	**773.3**	**812.3**	**891.4**	**918.0**	**1,041.6**
% NCR Consolidated Expense	≤60%	46.5	40.9	41.7	40.3	40.8	42.1	42.0	46.3
Executive Power	≤54%	43.0	38.1	38.8	36.7	38.2	39.4	38.9	43.5
Legislative Power	≤6%	3.6	2.9	3.0	3.2	2.6	2.5	2.8	2.5

* Figures adjusted by the Consumer Price Index – IPCA/IBGE.

Fiscal Sustainability Analysis

30. The fiscal situation of Recife projected for the period 2011-2027 aims at assessing the capacity of the MOR to deliver services to the population while assigning resources to the expansion of education and to public management, as well as repaying debt.

31. Projection exercises considered two scenarios. The baseline scenario, following present trend of deteriorating economic position of Recife in the state, shows a difficult situation, even if assumed a compromise of controlling personnel and goods and services. The loss of economic position and therefore tax and transfers revenue would reduce investment and jeopardize municipal infrastructure, throwing the MOR into a vicious circle. A second scenario, including the Bank operation, shows the importance of assigning part of the resources to improve public management, particularly fiscal management, in order to increase tax collection to cope with the additional resources needed to fund expansion of the education net.

C.1. Projected Fiscal Situation – 2011 to 2027

32. The assumptions of the projections are presented in Table 5. Inflation and GDP growth follow the market expectations, from the Central Bank Report – Market Readout. Debt estimates consider future disbursements of all the contracted loans as well as operations in negotiation with the Federal Savings and Loan Institution (*Caixa Econômica Federal* -- CEF), mostly related to infrastructure investments to prepare the City for the World Cup. On the expenditure side, equal amounts are added each year to investments financed out of MOR's own revenues and capital transfers, estimated for the initial years as 7 percent of NCR, following recent performance. We estimated debt repayment schedule based on MOR's information on operations conditions and distribution of disbursements. Conditions for Bank operation are also found in Table 5.

33. Hypothesis adopted for personnel and goods and services were conservative, avoiding the risk of unrealistic (good) results. Since the public sector is frequently subject to pressures to increase current expenses – mainly with personnel and with goods and services, we estimated those expenses as increasing at rates close to those used for revenues. While revenues are generally driven by the economic activity, expenses rarely expand just with population. Personnel expense increase has to do basically with services expansion, new benefits and increased productivity. Goods and services expense has to do mainly with services expansion and cost.

Table 5: Assumptions for Financial Projections

VARIABLES	ASSUMPTIONS
Macroeconomic/demographic	
Population growth	0.70% per year. Recife population average growth 2000-10 was 0,78% per year, federal bureau of statistics (IBGE)
GDP growth	4.0% for 2011, 4.1% for 2012, according to market expectations (FOCUS Report, Central Bank, May 20, 2011). In baseline scenario, 4% until 2015, 3.5% in 2016-20 and 3% in 2021-4. In scenario WB, 4% from 2013 on
Inflation rate	6.3% for 2011, 5.1% for 2012, according to market expectations (FOCUS Report, Central Bank, May20, 2011) and 4.5% for 2013 on
Exchange rate	R$1.62/US$1,00 for 2011, R$1.70/US$1,00 for 2012 (FOCUS Report, May 20, 2011) varying inflation difference afterwards
Revenue	
Taxes	
Urban Land and Property Tax -IPTU	increases with inflation and population; in scenario WB, additional growth of 10% in 2015 and another 10% in 2016, as a result of cadastres revision and reassessment of properties values
Tax on Services – ISS	increases with inflation and GDP growth; in scenario WB, additional growth in 2014 – 10% and 2015 – 5% as a result of tax administration measures
Income tax withhold at source -IRRF	increases with personnel expenditures
Social Contributions	increase with personnel expenditures
Others	increase with inflation and GDP growth
Intergovernmental Transfers	
Municipalities participation Fund- FPM	increases with inflation and GDP growth
Unified Health System – SUS	federal transfers increase with inflation and GDP growth, following criteria set in Constitutional Amendment nº 29 for federal expenses in health
ICMS	increases with inflation and GDP growth
IPVA	increases with inflation and population growth
FUNDEB	Contribution to the Fund is calculated according Federal Constitution, as 20% transfers of ICMS, FPM, IPVA, IPI-ex and LC87/76. Transfer from FUNDEB to the MOR is estimated as 80 % of MOR's contribution to the Fund (historic average). In scenario WB, expansion in early childhood education reduces losses and transfers reach 95% of contributions to the Fund from 2014 on.
Others	increase with inflation and population growth
Other Current Revenues	increase with inflation
Expenses	
Personnel, including social security benefits	increase with inflation and population growth plus 3% due to incorporation of benefits and to take into account (partially) the rule for minimum salary increase. In scenario WB in 2015 and 2016, additional increases of IPTU and ISS result in expansion of expenses with education and health to cope with constitutional floors. Two thirds of the extra expenses go to personnel and one third to goods and services related to education and health.
Goods and Services	increase with inflation and population growth plus 2.5% due to services expansion;
Investment (net of sale of non financial assets)	minimum amount equal to 7% of Net Current Revenue until 2020, adding investment financed by the new loans and disbursement of loans already contracted along 2011-4. In baseline scenario, from 2021 on, investment /NCR decreases sharply, until 1% in 2027. In scenario WB, besides investments financed by the new loans and disbursement of loans already contracted, minimum amount equal to 7% of Net Current Revenue until 2013, 8% in 2014, 9% in 2015-19 and 11% from 2020 on. Investment financed by the IBRD loan in 2012-25 is considered, besides those related to new loans and disbursement of loans already contracted.
Net Acquisition of Financial Assets	Zero
Debt Service	Estimated from information of the MOR regarding the contractual conditions for each operation and the schedule of disbursements from operations other than the IBRD. Taken into account all the operations under negotiation.
IBRD Loan	US$130.0 million, disbursed in 8 tranches in March-Sept 2012-15, Libor plus spread 1.05%, 30 years maturity, 17.5 years average maturity, 5 years grace period, 0.25% front-end fee

34. Scenario 1 is the baseline case and results are presented in Table 6.1 below. The GDP growth is reduced after the World Cup, following the recent trend above described of loosing position in the state economy. The lowest increase in revenues result in reducing investments, aggravating the deficiency in infrastructure, which is reflected in loss of economic activities, part of which would move to neighboring cities.

35. Debt indicators are kept under adequate limit, since, as above explained, the MOR has not taken significant amounts of loans in recent years. On the other side, personnel expenses approach the FRL prudential limit (90 percent x 60 percent). Besides that, increasing revenue rigidity makes difficult fiscal adjustment. To keep investments at least at the present level, Goods and Services would have to suffer additional decreases. Besides that, a tight control of personnel expenses would have to keep payroll growth according to inflation and population, what seems quite unrealistic.

36. In short, the assumptions adopted in this scenario make clear the need of expanding revenue and controlling costs to reduce infrastructure deficiencies and recuperate the city's position in the state economy. The State of Pernambuco is making a substantial effort to expand and modernize economic activity. Many industrial plants are being built in the neighboring cities. Recife may take advantage of the fact that it concentrates, in the region, modern services, like financial activities, IT, and other. The MOR needs to overhaul public management, to avoid losing opportunities. Attention should be put not only on fiscal matters, but also on project management. Many credit operations contracted years before (2006/2007) with the CEF to fund sanitation projects still have pending disbursements. The *Capibaribe Melhor*, a contract of US$32.8 million with the Bank in September 2009 still has R$54.0 million to be disbursed in 2011/2013, almost the total amount contracted. The substantial amount related to new credit operations to fund projects for the World Cup need an agile management to follow the tight chronogram of implementation.

37. The second scenario, the Scenario World Bank, projects the fiscal situation of Recife including the Bank operation of US$ 130.0 million, to be used mainly in expansion of the education net – US$100.0 million, but also in modernizing public administration. Improvement in tax management is one of the activities to be tackled. Impacts on revenues and expenses of those projects are considered in the projection. Results for 2011-2027 are presented in Table 6.2 below.

38. Cadastres revision and reassessment of properties values, but also measures to reduce evasion and increase efficiency on ISS collection must be firmly considered by municipal administration, notwithstanding political costs. The increase in the IPTU collection is a result of approving a reassessment of properties values in 2014. Additional increase of revenue in 2015 is related cadastres revision, also planned by the Prefeitura within the context of a IDB financed program called "PNAFM". Given the natural difficulties faced by municipalities in implementing those projects, and the importance of choosing the political moment to negotiate them, it's important to begin to design those projects as soon as possible. Municipalities have been doing much effort to modernize ISS tax collection. Differently from the IPTU, many initiatives in ISS do not require new legislation.

39. It's taken into account that resources assigned to tax management would result in increasing resources available to education and (and health) expenses. As there are not yet

estimates of the additional expenses needed to operate the expanded education net, there were assumed specific increases in personnel and goods and services to cope with it. Following constitutional rules, 25 percent of additional tax collection is assigned to education and another 15 percent to health actions, most of which are supposed to fund expenses in personnel and goods and services in those areas. These additional resources in education may fulfill, at least partially, the increased needs to manage the expanded net. It should be noted, however, the enormous importance of having accurate estimates of costs related to the investments intended with the Bank loan, since those are permanent expenses to be supported by the municipal Treasury. The accelerated increase in the number of students may raise the transfers received from FUNDEB, reducing present net loss in transactions with the Fund, as above described.

40. Assumed control of current expenditures, additional revenue permits the MOR to increase investments, filling the gap of infrastructure needed to take advantage of expected state economic development. Assignment of resources to payroll data systems would help to control personnel expenses as well as to evaluate risks related to the pension system. Modernization on debt control would reduce the risk of accumulating hidden liabilities that may jeopardize fiscal situation.

41. Compared to the baseline scenario, primary balance indicator is improved, notwithstanding the higher investment. Differently from baseline scenario, personnel expenses are stable around 46.3 percent, even in face of expansion of services provision. The ratio Net Debt/NCR is higher than in baseline scenario until 2018, given the Bank loan. For the same reason, the ratio Debt Service/NCR equals the baseline scenario only in 2022. As previously stated both indicators are under adequate levels.

Table 6.1 – Municipality of Recife Fiscal Balances – 2010 and 2011-2027

in R$ million current

	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	2025	2026	2027
I. REVENUE	**2,357.5**	**2,598.6**	**2,832.0**	**3,066.7**	**3,321.2**	**3,597.1**	**3,880.7**	**4,186.9**	**4,517.6**	**4,874.8**	**5,260.5**	**5,654.0**	**6,077.2**	**6,532.3**	**7,021.9**	**7,548.5**	**8,114.9**	**8,724.2**
Taxes	814.0	893.2	970.2	1,047.2	1,130.6	1,220.8	1,313.7	1,413.8	1,521.8	1,638.2	1,763.6	1,892.1	2,030.0	2,178.1	2,337.2	2,508.1	2,691.8	2,889.0
Social Contribuitions	83.9	92.5	100.9	109.5	118.8	128.8	139.7	151.6	164.4	178.3	193.5	209.8	227.6	246.9	267.8	290.5	315.1	341.8
Intergovernmental Transfers	1,303.5	1,443.7	1,579.5	1,716.6	1,865.6	2,027.5	2,192.9	2,371.8	2,565.3	2,774.6	3,000.9	3,230.0	3,476.6	3,742.1	4,027.8	4,335.3	4,666.3	5,022.6
Other Revenues	156.1	169.2	181.4	193.4	206.2	220.0	234.3	249.7	266.1	283.7	302.5	322.1	342.9	365.2	389.0	414.5	441.7	470.8
of which: interest on cash available	37.0	40.5	43.8	47.0	50.6	54.4	58.4	62.8	67.5	72.6	78.0	83.9	90.2	96.9	104.2	112.0	120.4	129.5
II. EXPENSE	**2,106.4**	**2,326.8**	**2,555.8**	**2,783.6**	**3,018.3**	**3,267.3**	**3,537.3**	**3,830.3**	**4,148.6**	**4,494.5**	**4,870.1**	**5,277.7**	**5,720.0**	**6,200.1**	**6,721.3**	**7,287.3**	**7,902.1**	**8,569.9**
Compensation of Employees	944.5	1,041.8	1,136.5	1,232.8	1,337.3	1,450.5	1,573.4	1,706.7	1,851.3	2,008.1	2,178.2	2,362.7	2,562.9	2,780.0	3,015.4	3,270.9	3,548.0	3,848.5
Pensions	199.2	219.8	239.7	260.1	282.1	306.0	331.9	360.0	390.5	423.6	459.5	498.4	540.6	586.4	636.1	690.0	748.4	811.8
Goods and services	954.5	1,047.8	1,137.5	1,228.0	1,325.6	1,430.9	1,544.7	1,667.4	1,800.0	1,943.0	2,097.5	2,264.2	2,444.2	2,638.5	2,848.2	3,074.6	3,318.9	3,582.7
Interest Payments	8.3	17.5	41.9	62.8	73.4	79.9	87.3	96.1	106.9	119.7	134.9	152.4	172.4	195.3	221.6	251.9	286.8	326.8
III. GROSS OPERATING BALANCE	**251.1**	**271.7**	**276.2**	**283.1**	**302.9**	**329.8**	**343.4**	**356.6**	**369.0**	**380.3**	**390.4**	**376.3**	**357.1**	**332.2**	**300.5**	**261.2**	**212.8**	**154.3**
(as a %of NCR)	11.2	11.0	10.2	9.7	9.6	9.6	9.3	8.9	8.6	8.2	7.8	7.0	6.2	5.3	4.5	3.6	2.8	1.9
IV. Investments	**167.5**	**443.5**	**444.8**	**312.2**	**227.1**	**240.0**	**258.9**	**279.3**	**301.2**	**325.0**	**350.6**	**322.9**	**346.9**	**310.6**	**267.0**	**287.0**	**154.2**	**82.8**
(as a %of NCR)	7.5	17.9	16.5	10.7	7.2	7.0	7.0	7.0	7.0	7.0	7.0	6.0	6.0	5.0	4.0	4.0	2.0	1.0
V. NET LENDING/BORROWING**	**83.5**	**(171.8)**	**(168.6)**	**(29.1)**	**75.8**	**89.8**	**84.5**	**77.4**	**67.8**	**55.3**	**39.8**	**53.4**	**10.2**	**21.5**	**33.5**	**(25.8)**	**58.6**	**71.4**
(as a %of NCR)	3.7	(6.9)	(6.2)	(1.0)	2.4	2.6	2.3	1.9	1.6	1.2	0.8	1.0	0.2	0.3	0.5	(0.4)	0.8	0.9
VII. NET INCURRENCE OF LIABILITIES***	**(81.3)**	**171.8**	**168.6**	**29.1**	**(75.8)**	**(89.8)**	**(84.5)**	**(77.4)**	**(67.8)**	**(55.3)**	**(39.8)**	**(53.4)**	**(10.2)**	**(21.5)**	**(33.5)**	**25.8**	**(58.6)**	**(71.4)**
Debt Amortizations	(47.1)	(63.2)	(70.9)	(81.7)	(78.8)	(73.3)	(74.3)	(73.0)	(67.9)	(61.0)	(61.5)	(63.5)	(65.8)	(68.3)	(71.0)	(67.3)	(70.3)	(72.9)
New Loans	23.5	270.1	255.8	107.5	5.5	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Fiscal Year Deficit****	(57.7)	(35.1)	(16.3)	3.3	(2.5)	(16.4)	(10.2)	(4.4)	0.1	5.7	21.6	10.1	55.6	46.8	37.5	93.1	11.7	1.4
NET CURRENT REVENUE - NCR	**2,248.3**	**2,478.0**	**2,700.4**	**2,923.9**	**3,166.2**	**3,428.9**	**3,698.4**	**3,989.3**	**4,303.5**	**4,642.6**	**5,008.9**	**5,381.5**	**5,782.1**	**6,212.8**	**6,675.9**	**7,173.9**	**7,709.3**	**8,285.0**
PRIMARY BALANCE	**52.5**	**(194.9)**	**(170.5)**	**(13.5)**	**98.5**	**115.2**	**113.3**	**110.6**	**107.0**	**102.4**	**96.6**	**121.8**	**92.3**	**119.8**	**150.8**	**113.9**	**224.8**	**268.6**
(as a %of NCR)	2.3	(7.9)	(6.3)	(0.5)	3.1	3.4	3.1	2.8	2.5	2.2	1.9	2.3	1.6	1.9	2.3	1.6	2.9	3.2
Credit Operations(as a % of NCR)	≤16%	10.9	9.5	3.7	0.2	-	-	-	-	-	-	-	-	-	-	-	-	-
Net Consolidated Debt (as a % of NCR)	≤120%	28.4	32.5	31.2	26.7	22.2	18.5	15.4	12.8	10.8	9.4	7.8	7.2	6.4	5.5	5.6	4.5	3.3
Debt service (as a %of NCR)	≤11.5%	3.3	4.2	4.9	4.8	4.5	4.4	4.2	4.1	3.9	3.9	4.0	4.1	4.2	4.4	4.4	4.6	4.8
Net Personnel expenses (as a % of NCR)	≤60%	47.2	47.2	47.3	47.4	47.5	47.7	48.0	48.3	48.5	48.8	49.3	49.7	50.2	50.7	51.2	51.6	52.1

Table 6.2 – Municipality of Recife Fiscal Balances – 2010 and 2011-2027

in R$ million current

	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	2025	2026	2027
I. REVENUE	**2,357.5**	**2,598.6**	**2,832.0**	**3,066.7**	**3,422.5**	**3,766.6**	**4,108.1**	**4,449.2**	**4,819.1**	**5,220.2**	**5,655.2**	**6,127.0**	**6,638.7**	**7,193.8**	**7,795.9**	**8,449.0**	**9,157.6**	**9,926.4**
Taxes	814.0	893.2	970.2	1,047.2	1,188.7	1,343.2	1,479.1	1,596.8	1,724.2	1,862.0	2,011.1	2,172.5	2,347.2	2,536.3	2,741.1	2,962.8	3,202.8	3,462.8
Social Contribuitions	83.9	92.5	100.9	109.5	118.8	128.8	139.7	151.6	164.4	178.3	193.5	209.8	227.6	246.9	267.8	290.5	315.1	341.8
Intergovernmental Transfers	1,303.5	1,443.7	1,579.5	1,716.6	1,908.8	2,074.5	2,254.6	2,450.3	2,663.0	2,894.1	3,145.3	3,418.3	3,715.0	4,037.5	4,388.0	4,768.8	5,182.8	5,632.6
Other Revenues	156.1	169.2	181.4	193.4	206.2	220.0	234.7	250.6	267.5	285.8	305.3	326.3	348.8	373.0	399.0	426.9	456.9	489.2
of which: interest on cash available	37.0	40.5	43.8	47.0	50.6	54.4	58.4	62.8	67.5	72.6	78.0	83.9	90.2	96.9	104.2	112.0	120.4	129.5
II. EXPENSE	**2,106.4**	**2,326.8**	**2,556.2**	**2,786.1**	**3,045.2**	**3,315.0**	**3,641.7**	**3,943.1**	**4,270.8**	**4,625.4**	**5,010.6**	**5,428.5**	**5,882.0**	**6,374.1**	**6,908.4**	**7,488.4**	**8,118.6**	**8,802.9**
Compensation of Employees	944.5	1,041.8	1,136.5	1,232.8	1,349.3	1,470.5	1,605.4	1,741.4	1,888.9	2,048.9	2,222.5	2,410.8	2,615.0	2,836.5	3,076.8	3,337.4	3,620.1	3,926.8
Pensions	199.2	219.8	239.7	260.1	285.1	316.0	343.9	373.0	404.6	438.9	476.1	516.4	560.2	607.6	659.1	714.9	775.5	841.2
Goods and services	954.5	1,047.8	1,137.5	1,228.0	1,332.6	1,440.9	1,594.7	1,721.4	1,858.2	2,005.9	2,165.4	2,337.5	2,523.3	2,723.9	2,940.4	3,174.1	3,426.4	3,698.7
Interest Payments	8.3	17.5	42.4	65.3	78.3	87.6	97.7	107.2	119.0	131.6	146.6	163.8	183.5	206.1	232.1	262.0	296.6	336.2
III. GROSS OPERATING BALANCE	**251.1**	**271.7**	**275.8**	**280.6**	**377.3**	**451.5**	**466.5**	**506.1**	**548.3**	**594.8**	**644.6**	**698.5**	**756.7**	**819.6**	**887.5**	**960.6**	**1,039.1**	**1,123.5**
(as a % of NCR)	11.2	11.0	10.2	9.6	11.5	12.5	11.9	11.9	11.9	11.9	11.9	11.9	11.9	11.9	11.9	11.9	11.9	11.9
IV. Investments	**167.5**	**443.5**	**498.7**	**368.1**	**324.2**	**382.6**	**353.3**	**382.6**	**414.4**	**448.8**	**594.2**	**643.8**	**697.5**	**755.7**	**818.9**	**887.5**	**961.9**	**1,042.6**
(as a % of NCR)	7.5	17.9	18.5	12.6	9.9	10.6	9.0	9.0	9.0	9.0	11.0	11.0	11.0	11.0	11.0	11.0	11.0	11.0
V. NET LENDING/BORROWING**	**83.5**	**(171.8)**	**(222.9)**	**(87.6)**	**53.1**	**68.9**	**113.2**	**123.5**	**133.9**	**145.9**	**50.4**	**54.8**	**59.3**	**63.9**	**68.6**	**73.1**	**77.2**	**80.9**
(as a % of NCR)	3.7	(6.9)	(8.3)	(3.0)	1.6	1.9	2.9	2.9	2.9	2.9	0.9	0.9	0.9	0.9	0.9	0.9	0.9	0.9
VII. NET INCURRENCE OF LIABILITIES***	**(81.3)**	**171.8**	**222.9**	**87.6**	**(53.1)**	**(68.9)**	**(113.2)**	**(123.5)**	**(133.9)**	**(145.9)**	**(50.4)**	**(54.8)**	**(59.3)**	**(63.9)**	**(68.6)**	**(73.1)**	**(77.2)**	**(80.9)**
Debt Amortizations	(47.1)	(63.2)	(70.9)	(81.7)	(78.8)	(73.3)	(74.3)	(82.8)	(78.0)	(71.4)	(72.1)	(74.4)	(77.0)	(79.7)	(82.7)	(79.3)	(82.6)	(85.5)
New Loans	23.5	270.1	309.7	163.5	62.8	58.8	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Fiscal Year Deficit****	(57.7)	(35.1)	(15.8)	5.8	(37.2)	(54.3)	(38.9)	(40.7)	(55.9)	(74.6)	21.7	19.7	17.7	15.8	14.1	6.2	5.5	4.5
NET CURRENT REVENUE - NCR	**2,248.3**	**2,478.0**	**2,700.4**	**2,923.9**	**3,267.6**	**3,598.4**	**3,925.7**	**4,251.2**	**4,604.2**	**4,987.0**	**5,402.1**	**5,852.3**	**6,340.6**	**6,870.3**	**7,444.9**	**8,068.1**	**8,744.2**	**9,477.8**
PRIMARY BALANCE	**52.5**	**(194.9)**	**(224.4)**	**(69.4)**	**80.7**	**102.0**	**152.3**	**167.8**	**185.3**	**204.9**	**118.8**	**134.5**	**152.5**	**173.0**	**196.3**	**222.9**	**253.2**	**287.5**
(as a % of NCR)	2.3	(7.9)	(8.3)	(2.4)	2.5	2.8	3.9	3.9	4.0	4.1	2.2	2.3	2.4	2.5	2.6	2.8	2.9	3.0
Credit Operations(as a % of NCR)	≤16%	10.9	11.5	5.6	1.9	1.6	-	-	-	-	-	-	-	-	-	-	-	-
Net Consolidated Debt (as a % of NCR)	≤120%	28.4	34.5	35.2	30.2	25.9	21.2	16.9	13.0	9.3	7.9	6.5	5.2	4.0	2.9	1.9	1.0	0.1
Debt service (as a %of NCR)	≤11.5%	3.3	4.2	5.0	4.8	4.5	4.4	4.5	4.3	4.1	4.0	4.1	4.1	4.2	4.2	4.2	4.	4.4
Net Personnel expenses (as a % of NCR)	≤60%	47.2	47.2	47.3	46.4	46.1	46.1	46.2	46.2	46.3	46.4	46.4	46.5	46.5	46.6	46.6	46.7	46.7

C.2. Sensitivity Analysis

42. Using the Bank operation as a baseline, a sensitivity analysis exercise was performed, aiming at identifying the major risks to future fiscal performance of Recife Municipal government. The analysis deals with risks related to revenues, mainly taxes and current transfers, expenditures – personnel and goods and services and to the exchange rate, since dollar indexed loans would have increasing participation on total debt. As debt indicators are still relatively low (even not so low if we compare Recife with similar municipalities) there would be needed huge changes to reverse the present situation of compliance with debt limits. That's why our analysis focus on personnel expenses/NCR and resources available for investments. As we pointed out in Scenario 1, the City needs to improve its fiscal capacity to release funds for investments, otherwise entering a vicious circle, undermining its growth and consequently its tax collection.

43. In addition of previous comments related to institutional aspects of municipal management, we point out some difficulties that may be faced by the MOR, affecting the implementation of the projects, most of which with negative fiscal impacts.

44. On the revenue side, if NCR decreased by 15 percent, personnel expenditures/NCR would climb to 60 percent. If economic growth was reduced from 4 percent a year to 2 percent a year since 2013, the indicator would reach 60 percent in 2023. Besides that, investments would follow to zero yet in 2018. If additionally the IPTU and ISS projects were not implemented. New reductions on NCR would anticipate the non compliance with FRL limits on personnel to 2020. Nevertheless, that would not be a possible position, since huge fiscal year deficits would require reducing personnel and /or goods and services expenses. As public servants have a stable position by law, the burden would have to be supported mostly by goods and services.

45. If economic growth was kept at 4 percent, but the IPTU and ISS projects were not implemented, personnel expenses would be kept around an average 52 percent of NCR and investments would hardly be higher than 6 percent of NCR, with all the negative impact on City's development already stated. As we see, investment is very sensitive to changes in personnel expenses and goods and services, since, except in the initial years where a major amount if financed by credit operations, investments represent just around 20 percent of personnel and 27 percent of goods and services.

46. The risk related to the exchange rate is not significant, since in 2015, after total Bank loan disbursement, the amount of debt in dollars would be around 20 percent and debt indexed to IGP-DI would be almost totally repaid (IGP-DI is affected by dollar variations through its wholesale price index component). A devaluation of 30 percent would increase debt by 6 percent. The effect on debt service would not be significant too.

47. Besides risks that affect total revenue and expenditure as well as its major groups: taxes, transfers, personnel, goods and services and investments, it should be pointed out some additional aspects. In 2010, the MOR registered R$442.0 million as expense with education, over the Constitutional limit of 25 percent (25.3 percent on own revenue and constitutional transfers, according to legislation). Childhood education absorbed R$30.0 million. If expense grew with inflation and economic growth, total amount for 2012-2015 would be R$165.0 million. Resources of Bank loan to be assigned to childhood education – around R$170.0 million would double the amount spent. It should also be considered the difference between managing permanent expenditures, for which there are

routines, already in practice (even deserving improvement) and investments, which require specific technical capabilities.

48. Along this analysis deficiencies in debt management were highlighted. Indirect administration debt is out of control and there may be hidden liabilities. Regardless of the establishment of stronger controls, it is necessary, immediately, to set controls on indirect administration debt and make clear the situation of INSS debt, which accounts for 85 percent of consolidated debt.