

Document of
The World Bank

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Report No 39931-BR

PROJECT APPRAISAL DOCUMENT

ON A

PROPOSED LOAN IN THE AMOUNT OF US\$18.90 MILLION

TO THE

MUNICIPALITY OF PELOTAS

WITH A GUARANTEE EACH FROM THE FEDERATIVE REPUBLIC OF BRAZIL

IN SUPPORT OF THE SECOND PHASE OF THE US\$66 MILLION

RIO GRANDE DO SUL INTEGRATED MUNICIPAL DEVELOPMENT PROGRAM
(PDMI)

November 21, 2007

Sustainable Development Department
Brazil Country Management Unit
Latin America and Caribbean Region

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Annex 16: Appraisal Document for Municipality of Pelotas

BRAZIL: RIO GRANDE DO SUL INTEGRATED MUNICIPAL DEVELOPMENT PROGRAM

1. Municipal Overview

The city of Pelotas is located in the southeastern part of the State of Rio Grande do Sul, approximately 252 km from the state capital, Porto Alegre. Pelotas is the third largest city in the state with a population of around 335,000 inhabitants, of which 93% live in urban areas. The overall density is average, with around 196 inhabitants per Km².

At the end of the 18th Century, Pelotas started its first period of substantial growth as a result of cattle raising in and around the settlement of São Pedro de Pelotas. It became famous for the production of *charque*, or jerked beef. The work was usually done by slaves. Sales of beef and beef derivatives to the states of São Paulo, Rio de Janeiro and Minas Gerais prospered and by 1830, with the growing population, the town of Pelotas was awarded the status of “city,” with its own municipal government. Further expansion of cattle-raising activities in the area transformed Pelotas into the economic leader of the province.

During the mid-20th century, the former dynamic regional jerked beef industry faced successive severe crises, due to lack of appropriate technology, problems in adapting more productive cattle breeds in the region, increasing labor costs and labor regulation, as well as strong competition from Uruguayan production. More recently, a number of large fruit-processing plants have closed down—after having operated for decades in the municipality—which eliminated thousands of formal jobs. Poverty, informality and unemployment have since become big issues in the municipality.

Nearly 21.8% of the municipal population is considered poor (2000), almost double the corresponding figure for the state capital Porto Alegre (11.3%). Also, a recent survey indicates that 20.8 % of the economically active population of the Pelotas region was unemployed, compared to 13.7% for the Porto Alegre Metropolitan Area.¹

According to the State Statistics Agency (FEE), total value added municipal GDP in 2004 was nearly US\$ 1.Billion and per capita GDP reached US\$3,185, about half of the state’s average (US\$ 6,054). Municipal GDP has experienced a slight decline over recent years, and Pelotas has been dropping in the economic ranking of the State. Nearly 85% of industrial GDP relates to traditional industries, such as food processing, leather, fertilizers and other inputs for agriculture.

¹ Pesquisa de Emprego e Desemprego-PED, produced by DIEESE and the Federal Ministry of Labor (Nov 2006).

Table 1. GDP- 2004 (US\$ 1,000)

	Agriculture	Industry	Service	Total	Per capita GDP US\$ 1
Pelotas	64.399	333.983	609.615	1.007.996	3.185
State of RS	10.060.752	26.266.087	25.243.209	61.570.049	6.054

Source: FEE

Over the years, Pelotas has become an important commercial center, attracting customers from neighboring regions to its nearly 7,500 commercial establishments (shops, banks, insurance firms, currency exchange bureaus and transport operators) that employ around 60% of the city's labor force.

Currently, the main economic activities in Pelotas are:

- (i) Agricultural sector (6.4% of GDP): rice, corn, beans, tomatoes, potatoes, oranges, peaches, beef, pork and poultry;
- (ii) Industrial sector (33% of GDP): food processing, nonmetallic minerals, metalworking, ceramics, chemical products, clothing, footwear and textiles;
- (iii) Commercial sector (60.5% of GDP): wholesale and retail trade and the transport sector.

The Autonomous Water and Sewerage Service of Pelotas (SANEP) is responsible for collecting and treating sewage, providing water and urban drainage, and the collection and disposal of solid waste throughout the municipal area. SANEP distributes 86.5 million liters of potable water to 99% of the city's population. The water supply network of 857km reaches 103,556 households. The system consists basically of three treatment stations, 20 reservoirs, feeder pipelines and distribution networks.

The 349 km of sewer networks only serve 67% of the households and businesses in the city, and only 26% of the collected waste water is properly treated in two treatment plants. The lack of treatment and proper drainage, results in increasing problems with flooding, pollution of the water bodies, as well as odor problems. Regarding solid waste, 150 tons are collected daily and disposed in controlled landfills.

The roads in the municipality are in poor state, especially in and around the downtown area. The streets need to be rehabilitated considering the high traffic volumes entering the city every day. Many streets are unpaved and open gullies carry storm- and wastewater, causing problems in a number of areas of the city.

2. Results Framework and Monitoring

The key results and outcomes to be monitored during project implementation are:

Table 2. Project Development Objectives and Outcome Indicators

Project Development Objectives	Outcome Indicators	Use of Outcome Information
<p>Improve the capacity of the municipality of Pelotas, to provide infrastructure services and employment opportunities for its population.</p> <p>Enhance municipal learning and knowledge sharing with the other 5 municipalities participating in the PDMI.</p>	<p>Improved Municipal Management Capacity</p> <ul style="list-style-type: none"> • Number of municipal projects institutionalizing improved evaluation, social and environmental management processes in the municipal government of Pelotas • Percentage of citizens satisfied with quicker and more user-friendly access to client services provided by the municipality • Number of good practices or innovations replicated from other municipalities <p>Increased local economic development opportunities</p> <ul style="list-style-type: none"> • The net percentage increase in formal jobs is higher (or its decrease is lower) among the beneficiaries of the project than in the municipal economy as a whole • The net percentage increase in formal firms is higher (or its decrease is lower) among the beneficiaries of the project than in the municipal economy as a whole <p>Improved Infrastructure Services</p> <ul style="list-style-type: none"> • Number of rural people with coverage of water supply • Reduction in the density of vehicles and increase in their average speed in selected avenues benefitted by the project • Percentage of urban citizens satisfied with the quality of infrastructure services 	<p>Monitoring, evaluation and adjustment of each municipal policies, management processes and programs</p>
Intermediate Results	Intermediate Results Indicators	Use of Intermediate Results
Municipal Capacity	<ul style="list-style-type: none"> • Implementation of information systems for municipal databases • Number of municipal staff trained • Percentage of annual work program delivered on time 	<p>Monitoring of project implementation and timely intervention with corrective measure as needed</p>
Income and Employment Generation	<ul style="list-style-type: none"> • Number of beneficiaries of training and/or technical assistance • Number of micro-credit loans reaching target population • Number of productive infrastructure installed 	

Infrastructure Services	<ul style="list-style-type: none"> • Physical progress of infrastructure improvements in urban transport as a percentage of km of paved/rehabilitated roads and substituted, rehabilitated or duplicated bridges • Physical progress of urban improvements and environmental recovery as a percentage of target attained: m2 of green areas recovered • Physical progress of water, sanitation and drainage infrastructure improvements in absolute numbers and as a percentage of target attained: km of water supply network, km of sanitation network 	
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Arrangements for results monitoring

Data Collection and Reporting: The municipality, through the UGP, will submit quarterly progress reports to the UAP and a bi-annual progress report to the Bank, a month before the supervision mission. The municipality will put in place a project Management Information Systems (MIS) and Monitoring and Evaluation System (M&E) and the UGP will manage both systems and collect relevant data from the respective implementing secretariats and organize necessary surveys each year to monitor and evaluate the progress of the project. The indicators related to the WSS improvements will be the responsibility of SANEP.

Table 3. Project Outcome Indicators, Baseline and Targets

Program Outcome Indicators	Baseline	Target	Target Cumulative Values				
			YR1 %	YR2 %	YR3 %	YR4 %	YR5 %
Number of municipal projects institutionalizing improved evaluation, social and environmental management processes in the municipal government of Pelotas	0	At least 3 projects institutionalize improved processes	0	0	1	2	3
Percentage of citizens satisfied with quicker and more user-friendly access to client services provided by the municipality	0	70%	0	40%	50%	60%	70%
Number of good practices or innovations replicated from other municipalities	0	At least 3 good practices or innovations replicated	This indicator will start to be measured after the UAP is working				
	To be calculated yearly	At least 10% above the performance of the municipal economy as a whole	0	3% above yearly	5% above yearly	10% above yearly	10% above yearly
The net percentage increase in formal firms is higher (or its decrease is lower) among the beneficiaries of the project than in the municipal economy as a whole	To be calculated yearly	At least 10% above the performance of the municipal economy as a whole	0	3% above yearly	5% above yearly	10% above yearly	10% above yearly

Number of rural people with coverage of water supply, percentage of treated wastewater	Coverage of water supply: 2000 rural people. 26% of collected wastewater treated	Coverage: 2000 rural people attended by water supply, 65% of wastewater treated.	water supply : 0	500	1000	1500	2000
			waste water treated : 26%	40%	65%	65%	65%
Reduction in the density of vehicles and increase in their average speed in selected avenues benefitted by the project	TBD at the beginning of project	Reduction by 20% in density and increase by 10% in speed – in avenues receiving interventions and roads nearby	Dens 0	0	-10%	-15%	-20%
			Speed 0	0	+5%	+7.5%	+10%
Percentage of urban citizens satisfied with the quality of infrastructure services	0	70%	0	0	50%	0	70%

Table 4. Intermediate Outcome Indicators, Baseline and Targets

Intermediate Outcome Indicators	Baseline	Target	Target Cumulative Values				
			YR1	YR2	YR3	YR4	YR5
Component 1: Number of properties cadastral in automated information systems	0	GIS and updated cadastre of 57,000 properties		10,000	25,000	40,000	57,000
Number of municipal staff trained	0	1000	50	200	600	1000	1000
Percentage of annual work program delivered on time	0	90% EOP	50%	60%	70%	80%	90%
Component 2: Number of beneficiaries of training and/or technical assistance	0	500 cluster firms and street vendors, 200 rural producers. Technological Park: 5 innovative firms, 10 incubated firms	50	150	300	450	500
			50	100	150	200	200
			1	2	3	4	5
			2	4	6	8	10
	0	500 per year	0	200	300	500	500
Number of productive infrastructure installed	0	Agrobusiness cluster: 1 packing house. Street vendors: enlargement of 1 Commercial Centre for Social Inclusion (Camelódromo). 1 Technological Park	0	Camelódromo	Packing House, Technology Park		
Component 3: Physical progress of infrastructure	0	55 km of paved/rehabilitated roads;	Roads 5	20	40	50	55

improvements in urban transport as a percentage of target attained: km of paved/rehabilitated roads; km of maintained roads; number of substituted, rehabilitated or duplicated bridges		1200 km of rural roads maintained; 19 bridges	Maintenance 100	400	800	1000	1200
			Bridges 1	5	10	15	19
Physical progress of urban improvements and environmental recovery as a percentage of target attained: m2 of green areas recovered	0	1 park with 3700 m2 of green area	0		3700 m2 of green area		
Physical progress of water, sanitation and drainage infrastructure improvements in absolute numbers and as a percentage of target attained: km of water supply network, km of sanitation network, number of wastewater treatment facilities	0	Expansion of 20 km of water supply network in rural areas. Construction of 3,2 km of water conveyance system in urban areas. 1 treatment wastewater facility	Water 5	10	15	20	20
			Conveyance 0	0	3,2	3,2	3,2
			Treatment 0	1	1	1	1

3. Project Description

Pelotas has the largest project of the PDMI with a wide range of related investments. The interventions have been carefully designed to complement other municipal projects, some of which involve external funding.

The Municipal Strengthening Component is a priority for the current administration and builds on efforts initiated under PMAT. One of the main investments will be the transformation of an existing office building downtown into a modern and efficient facility that will host most municipal secretariats. This will be complemented by additional computer system support and staff training to streamline municipal functions. Capacity will also be built across the municipal secretariats to implement improved fiduciary, social and environmental management processes in infrastructure projects. The Income Generation Component will assist in the formalization of street vendors, strengthen fruit and vegetables clusters sectors, and transform an abandoned factory into a state-of-the-art Technology Park that will foster research, product development and innovation, based on a combined effort of the public and private sectors and academia. The Infrastructure Services Improvement Component will invest in road rehabilitation, focusing on streets served by public transport, and expand water supply and sanitation services, while strengthening the capacity of the municipal water company, SANEP.

Detailed Project Description

Component 1: Municipal Strengthening: This component will improve the municipality's capacity to more effectively and efficiently execute projects, with a focus on fiduciary, environmental and social aspects, and improve the quality and efficiency of public services provided by the municipal government.

- **Sub-component 1.1: Public Service Modernization** to improve the municipality's capacity to more effectively and efficiently execute activities, especially related to client services. The project will finance the transformation of a municipal-owned a commercial building downtown into the new Municipal Administrative Centre. The key expected outcomes are: a modern and well equipped Municipal Administrative Center, reduction in administrative costs of the municipal government, improved quality and satisfaction of services to clients and citizens and integrated databases used by different municipal agencies, improved maintenance and overall quality of basic sanitation infrastructure (also supported by Component 3). Activities include:

 - a. Renovation of a municipal owned building into the new administrative center, provision of equipment and capacity building of staff in information technology and management (100% counterpart)
 - b. Installation of about 5 energy efficient automatic drainage pumps to reduce electricity consumption of the municipal government (100% counterpart)
 - c. Preparation of a master plan for drainage, water and sanitation, implementation of a municipal GIS system, completion of the works for the new administrative center, acquisition of about 24 vehicles for use by municipal government and provision of training and technical assistance to the Borrower's staff on topics related to municipal management and project implementation.

- **Sub-component 1.2. Project Management.** This subcomponent will finance activities to help coordinate and monitor project implementation and ensure fiduciary and safeguard aspects are adequately taken care of during project implementation. The key results will be proper project implementation and timely submission of financial reports, progress reports, environmental monitoring reports, etc. Outcomes include: successful implementation of the project; improved capacity of the municipality to prepare and monitor project implementation; integration of project-specific procedures in other municipal projects (especially fiduciary and safeguards) and enhanced learning through knowledge sharing with the other municipalities in the program. Activities that will be financed are:

 - a. Equipment and furniture required for the UGP, including acquisition of a vehicle, technical assistance, hire specialized consultants to supplement municipal staff and cover incremental operating costs for the municipality, dissemination, training and contribution to the UAP.

Component 2: Income and Employment Generation: The project will support cross-cutting activities to improve the overall business environment, facilitate access to micro-credit, cluster development for street vendors and fruit and vegetable producers in urban and rural areas and a Technology Park to promote R&D. Interventions will be grouped into two sub-components, as described below.

- **Component 2.1 Sustainable LED Strategic Work, Access to Micro-credit and Support to SME Clusters.** This sub-component will enhance municipal capacity to plan and implement sustainable LED strategies. Studies will be undertaken to assess the local business environment and devise measures to overcome key barriers, including for business registration. In addition, the sub-component will support the generation of employment and income through facilitating micro and small business access to micro-credit and improve their effectiveness through organization, training, technical assistance and preparation of business plans. Selected SME clusters will be provided with minimal infrastructure, technical assistance, technology and equipment upgrade, training and creation of brand names.

 - a. In terms of **strategic planning**, the project will support studies on: the municipality's growth potentials, business environment, identification of possible local growth engines and identification of regulatory/administrative barriers for business development. The expected outputs include the design and implementation of an LED Plan and enhanced local competitiveness.
 - b. **Support to Micro-business:** the project will help facilitate access to credit of about 500 small businesses per year and conduct training activities focused on business management, marketing, and organization of productive groups. Expected results include micro-enterprises using business plans, reduction of informality and reduction of mortality rates of micro-enterprises.
 - c. **Commercial Center for Social Inclusion (*Camelódromo*):** the project will help renovate a commercial facility and a nearby public park (Praça Cipriano Barcelos) to allow for the relocation of about 200 vendors to reduce informality. Support to this investment will be contingent on a solid business and facility management plan approved by the World Bank.
 - d. **Support to Agro-industry Cluster:** will include the construction of a packing-house, organization and training of about 500 beneficiary farmers and creation of a brand name associated to quality and origin of products thereby expanding the value-added of agriculture-based products and gaining access to high-end markets. Support to this investment will be contingent on a solid business and facility management plan approved by the World Bank.

- **Component 2.2 Technology Park:** This sub-component will finance the creation of a Technology Park and enhance collaboration on R&D across the many public, private and academic organizations that are located in the municipality but are currently not working systematically together. A building will be renovated and transformed into an establishment for private and academic sectors to foster innovative applied research and develop new technologies. A public-private partnership will create and support a development agency that will manage the park. Expected results will be a more innovative business environment and more successful business start-ups. Investment in this activity will require a sound business plan approved by the World Bank. Main investments:

 - a. Technology Park with about 5 innovative firms and incubator for about 10 businesses
 - b. 5 Centers for Digital Inclusion and a network connecting key locations in Pelotas, including municipal government offices.

Component 3: Infrastructure Services Improvements

- **Sub-component 3.1. Rehabilitation of urban road infrastructure and landscaping:** The sub-component will improve downtown road infrastructure and traffic planning, focusing on improved access by public transport, rehabilitation of downtown parks and landscaping, as well as renovation of historic buildings. Special attention will be given to traffic calming, pedestrian facilities and overall urban upgrading along the routes. The project will help establish better maintenance planning and operation to ensure long-term sustainability of investments. Some key investments of the sub-component are:
 - a. Renovation of selected historic buildings (*100% counterpart*)
 - b. Construction of approximately 50 bays for bus stops and approximately 10 pedestrian crossings (*100% counterpart*)
 - c. Rehabilitation of approximately 7,000 m² of streets and paving 1km of São Paulo street (*100% counterpart*)
 - d. Rehabilitation of approximately 3,700 m² of green space in the downtown area, paving and/or rehabilitation of main public transport access corridors, including pedestrian and bicycle infrastructure and landscaping.
- **Sub-component 3.2. Rehabilitation of rural road infrastructure and landscaping:** This sub-component will help improve access and reduce transport costs in rural areas through improved public transport services and reduction in operational costs. The sub-component will also help establish better maintenance planning and operation to ensure long-term sustainability of investments. The main investments of the sub-component will be the:
 - a. Acquisition of 10 trucks and 6 construction vehicles (*100% counterpart*)
 - b. Replacement of about 12 small bridges, rehabilitation of about 5 bridges and duplication of about 2 bridges and rehabilitation and improved maintenance of the core rural road network.
- **Sub-component 3.3. Urban Upgrading and Environmental Rehabilitation:** This sub-component will finance the expansion of the water supply network in rural areas and reduce potential problems with lack of water supply in urban areas with the construction of additional water conveyance systems. The project will reduce environmental impact on the *Canal São Gonçalo* and connected water bodies with the implementation of a wastewater treatment facility near the city center. The investments will be supported by a WSS management plan (prepared under Component 1), improved monitoring and maintenance of the sanitation network and improved management by SANEP. The expected outcomes include: improved water quality of local water bodies, reduction in water-borne diseases, improved maintenance and quality of sanitation service delivery. The main activities include:
 - a. Construction of water main to connect Arroio Pelotas with Sinott (*100% counterpart*)
 - b. Implementation of automated urban drainage system (*100% counterpart*)
 - c. Construction of waste water treatment facility, and expansion of the water supply system network in rural areas.

4. Project Costs

Table 5. Project costs by component

Components	Local (US\$ M)	Foreign (US\$ M)	Total (US\$ M)
1. <u>Municipal Strengthening</u>			
1.1 Public Service Modernization	3.32		3.32
1.2 Project Management	0.99		0.99
2. <u>Income and Employment Generation</u>			
2.1 Strategies, SME and Cluster Support	1.25		1.25
2.2 Technology Park	0.93		0.93
3 <u>Infrastructure Services Improvements</u>			
3.1 Urban Road Upgrading	17.76		17.76
3.2 Rural Road Upgrading	3.01		3.01
3.3 Water and Sanitation Services	3.49		3.49
Unallocated and Contingencies	0.70		0.70
Front-end fee	0.05		0.05
Total Project Costs	31.50		31.50

Table 6. Financing Plan for Pelotas

Components	World Bank (US\$ M)	Municipality (US\$ M)	Total (US\$ M)
1. <u>Municipal Strengthening</u>			
1.1. Public Service Modernization	1.00	2.32	3.32
1.2. Project Management	0.74	0.25	0.99
2. <u>Income and Employment Generation</u>			
2.1. Strategies, SME and Cluster Support	0.94	0.31	1.25
2.2. Technology Park	0.70	0.23	0.93
3. <u>Infrastructure Services Improvements</u>			
3.1. Urban Road Upgrading	11.36	6.40	17.76
3.2. Rural Road Upgrading	1.22	1.79	3.01
3.3. Water and Sanitation Services	2.19	1.30	3.49
Unallocated	0.70		0.70
Front-end fee	0.05		0.05
Total Project	18.90	12.60	31.50

C. Project Activities financed 100% by counterpart funds

Expenditures for selected activities financed 100% by the municipality and incurred after June 30, 2006 will be recognized as counterpart funding for the project provided that: (i) the activities are included in the list below, (ii) the Bank considers that the activities and costs are reasonable and necessary for the project, (iii) the Bank is satisfied with the procedures followed by the municipality for the procurement of the activities, and (iv) the Bank is satisfied that environmental and social requirements were adequately addressed. The activities are identified below:

Table 7. Activities with 100% counterpart funding:

Activity	Outputs	Funding Source	Cost, US\$, M
1.1 Public Sector Modernization	1.1-a. Renovation of the new administrative center, equipment and capacity building of staff.	<i>PMAT</i> : Contract No. 04.2.424.2.1 with BNDES	1.64
	1.1-b. Installation of five more energy efficient automatic drainage pumps	Contract No. 9928854 between SANEP and CEEE	0.35
3.1. Urban Road Upgrading	3.1-a. Renovation of historic buildings	<i>Programa Monumenta</i> : Covenant No. 392/2002 with Ministério da Cultura	1.90
	3.1-b. Construction of bays for bus stops and pedestrian crossings	<i>PRO-MOB</i> : Finance Ministry Authorization Law No. 5,260 with Caixa Estadual S/A- Agência de Fomento – RS	0.37
	3.1-c. Rehabilitation of 7,247 m ² of streets and paving of 1 km of streets	<i>CIDE</i> : Federal Law No. 10,336 with Ministério da Fazenda	0.37
3.2. Rural Road Upgrading	3.2-a. Acquisition of trucks & machines	<i>Pro-Vias</i> : Contract No. 026/2007 with BANRISUL- Banco do Estado do Rio Grande do Sul S/A	1.38
3.3. Water and Sanitation Services	3.3-a Water main to connect Arroio Pelotas with Sinot Station.	Contract No. 0215121-09/2006 with Ministério da Integração Nacional	0.42
	3.3-b Implementation of automated urban drainage system	Contract No. 0194141-71/2006 with Ministério das Cidades through the Caixa Econômica Federal-CEF	0.17
Total:			6.60

3.1 Urban Road Upgrading	•	•	•	•			•	•	★	
3.2 Rural Road Upgrading	•	•				★				
3.3 Water and Sanitation Services	•	•				•				★

SCP – Municipal Secretary of Coordination and Planning (Sec. de Coordenação e Planejamento); SAF – Municipal Secretary of Administration and Finance (Sec. de Administração e Finanças); STT – Municipal Secretary of Security, Traffic and Transport (Sec. de Segurança, Transporte e Trânsito); SMU – Municipal Secretary of Urban Services (Sec. de Urbanismo); SMG – Municipal Secretary of Government (Sec. de Governo); SDR – Municipal Secretary of Rural Development (Sec. de Desenvolvimento Rural); SDE – Municipal Secretary of Economic Development (Sec. de Desenvolvimento Econômico); SQA – Municipal Secretary of Environmental Quality (Sec. de Qualidade Ambiental); SMO – Municipal Secretary of Works (Sec. de Obras); SECULT – Municipal Secretary of Culture (Sec. de Cultura).

Project Coordinating Unit

The UGP was established by Municipal Law n° 5.302, of 28 December 2006 (copy is available in project files). It is located and depends upon the Secretariat of Planning. The UGP will be in charge of coordinating activity projects across the different secretariats, supervising works, and approving payment requests of implementing agencies. Regular meetings will be organized with the Municipal Secretaries. More complex and strategic issues will be addressed during weekly meetings of the relevant Municipal Secretariats.

The specific functions of the Pelotas PGU are to:

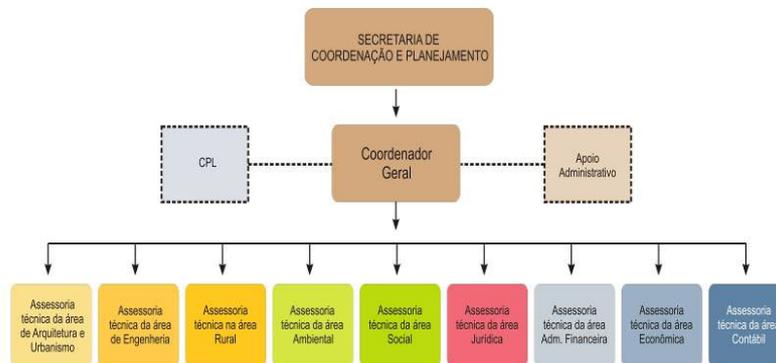
- Prepare and coordinate the execution of the municipal project implementation and procurements plan in conjunction with respective implementing municipal secretariats or departments. The procurement and implementation plans must be updated whenever necessary and at least once a year;
- Sequence and coordinate the execution of the works, services and procurement set forth in the Project Implementation Plan;
- Prepare the Monitoring and Evaluation Plan in order to monitor and evaluate the progress and achievements of the various projects on the basis of the outcome and impact indicators contained in the Logical Framework;
- Construct a database which will supply data for the different decision-making levels;
- Prepare technical and financial progress reports on the various project activities;
- Be responsible for financial management and generate the respective financial reports in order to ensure that all expenditure conforms to World Bank fiduciary and eligibility criteria. The financial management report system will be interlinked with the normal procedures employed by the municipality;
- Maximize the utilization of existing funds and resources and to seek new funding sources;
- Promote the dissemination of information on the project and its results to the community in general;
- Organize and deliver capacity building activities for technical staff of the municipalities and other beneficiaries of the project

Composition and Organogram

Project Coordination Unit and Staffing

The organizational structure of the UGP will comprise a General Coordinator and Technical Staff for Architecture, Engineering, Environment, Social, Rural, Accounting, Legal, Financial Management, Economics and an assistant for administrative support. Of the 10 members of the UGP planned for at project launch, seven staff will be seconded for other municipal secretariats and three consultants will be hired. The functions of each member of the UGP are described in the PDMI PAD and Operational Manual.

Organograma da Unidade Gestora de Projetos - UGP



6. Financial Management Risk Assessment and Arrangements

A financial management risk assessment² and arrangements for the municipality of Pelotas was carried out in loco on September 25-27, 2006 and January 08-09, 2007 and on September 13, 2007³. They are also based on the implementation arrangements presented in Annex 6 of the Program PAD and the detailed project description described in Annex 4 of the Program PAD. Even though individual ‘mini-PADs’ have been prepared for each loan, the overall Financial Management Arrangements for the Project, together with the FM arrangements for each of the four borrowers are summarized in Annex 7 of the Program PAD.

Conclusion of the FM assessment: Pelotas financial management, satisfy the Bank’s minimum requirements and has acceptable financial management and disbursements arrangements in place to adequately control, manage, account and report about the funds to be allocated to this Project.

The overall financial management risk associated with this project is considered *Substantial*, mostly related to the municipal and Implementing Agency capacities and lack of experience in the implementation of the financial management arrangements

² Based on the Bank’s FM guidelines - Financial Management Practices in World Bank Financed Investments Operations as of Nov 03, 2005 and other WB FM and Auditing documents.

³ to review the FM arrangements and provide first training to staff.

required by the Bank. Municipal However, with the arrangements and the action plan listed below, the remedial risk is rated as Moderate, enabling to provide relevant, timely and reliable information on it's implementation, allowing the Bank to take pro-active actions to mitigate the associated risks, as shown in the Risk Framework below. There is no FM related condition of effectiveness.

Strengths for project execution include: a) the commitment of the municipality to the project, b) good public sector FM arrangements in place; c) a supportive internal audit department, which checks all municipal transactions

Table 10. Project Risks and Mitigation Measures

Risk	H	S	M	L	Risk Mitigation Measures
Inherent Risks					
Country specific				X	
Sub-national (state) level			X		
Entity specific		X			No prior experience. Arrangements agreed to be closed follow up through Bank Supervision missions
Project specific			X		
Overall Inherent Risk			X		
Control Risks					
Implementing Agency		X			
Flow of Funds		X			SOE disbursed based.
Staffing		X			Training in Bank financial management will be provided to UGP's staff to be involved in the project financial management matters immediately following project effectiveness.
Accounting procedures			X		
Internal/External Audit			X		
Information Systems			X		Although good FM system, needs to be updated to assure adequacy with project description
Reporting & Monitoring		X			information/accounting system (SIM) is not ready to produce the said reports. It was agreed that the UGP will contact FATEC (responsible to develop the system) to find out the best alternative to run the said reports.
Overall Control Risk		X			

H-High S-Substantial M-Moderate L-Low

In order to mitigate the risks posed by the above-mentioned weaknesses includes: a) close supervision by the Bank FM team during the first year of project implementation will be required, b) Training in Bank financial management and disbursement procedures will be provided to UGP's staff to be involved in project financial management matters immediately following project effectiveness, c) creation of a central unit (UAP) in Porto Alegre will be created to provide technical assistance to the UGPs, d) Operational Manual, which shall include all financial management details (prior approved by the Bank) and e) review of internal control annual audit report, e The IFRs, SOE and SS were

explained in details using the LOA and POA codes and accounts. The client connection presentation was provided.

Project Coordination Unit and Staffing for FM

Civil servants of the Municipality of Pelotas will be relocated to the UGP as soon as the project has become effective and will be complemented with consultants as needed. The UGP will be responsible for all FM and disbursement aspects related to the implementation of the project, and will have an accountant in charge of overseeing financial management matters under the project, as outlined in the PDMI Operational Manual with charts and details of all financial management functions and routines undertaken through UGP's procedures.

The UGP will liaise with the UAP and all relevant secretariats to manage and use the project's resources and will also prepare IFRs for reporting purposes.

Budgeting

The UGP will have the responsibility of the preparation of the annual budgetary request for project funding. The budgeting process necessary for project implementation and disbursements is consolidated by the "Secretaria de Coordenação e Planejamento da Prefeitura Municipal de Pelotas". The information flows is through SIM – "Sistema de Informações Municipais", the municipality's budgetary tool, where all public expenditures are compulsorily budgeted for, committed and recorded, and through which all payments are made. Budgetary allocations for all project components will be made under Secretaria de Coordenação e Planejamento's budget, but earmarked for use by the respective project beneficiaries. Project funds will be made available and released through SIM.

Accounting, information system

The SIM was acquired from FATEC - Fundação de Apoio Tecnológico, public entity linked to the University of Santa Maria, RS. The SIM was developed by the municipal public information system's company COINPEL (Cia Informática de Pelotas) in order to improve the reporting framework. The municipality has the copyright of the system and IT support is carried out by COINPEL. The currently functioning modules of the system are protocol, budget and financial administration, general services, public module and human resources.

The municipality's budgeting process necessary for project implementation and disbursements will use the same IT system (SIM) as the Municipality. A specific cost center will be created in the municipal budget in order to provide the required project financial information by component/activity. The IFRs will also be issued through this system. COINPEL is responsible for IT support and operational and maintenance costs are charged through COINPEL's cost center.

The municipality will also develop monitoring module to evaluate the project's physical performance. The UGP will be in charge of monitoring activities of the project.

Financial Reporting – IFRs

The UGP will prepare quarterly IFRs for management and reporting purposes as detailed in the PDMI Operational Manual and the Umbrella PAD, with expenditures figures to be stated by quarter, accumulated for the annual and accumulated for the project. IFRs will be submitted to the Bank up to 45 days after the closing of each quarter:

IFR 1A – Source and application of funds by cost category as per Project Agreement,

IFR 1B - Statement of Investments by Components and activities,

Internal Audit

CAGEMP (Controladoria e Auditoria Geral do Município de Pelotas), which is linked to the Mayor's Office and performs ex-post controls for the municipality, will conduct the internal audit function of the project in accordance to the procedures outlined in the PDMI Operational Manual. A copy of this report will be sent to the WB by the end of each calendar year. This report will be assessed jointly with the external audit report and the IFRs to allow the Bank to have more information on project implementation and associated risks.

External Audit

The UGP will be responsible to provide the Bank annually with consolidated financial statements for the project including use of counterpart funds, audited by an independent auditing firm acceptable to the Bank, and under terms and conditions satisfactory to the Bank, which will include an opinion on the project financial statements and a management letter on the internal control structure. Procedures for this audit are detailed in the PDMI Program PAD and the Operational Manual. The Municipality of Pelotas is also audited, ex post, at least once a year, by the state's Court of Auditors- TCE-RS.

Disbursements and Flow of Funds

An operational account in R\$ will be opened in a commercial bank. Payments for works, goods and services will be made directly from this account for eligible payments to suppliers and contractors for project expenditures similar to other expenditures. Counterpart funds will be disbursed directly from the Municipal Treasury's single account to contractors and service providers.

The Borrower will open, maintain and operate under conditions acceptable to the Bank, a Designated Account in US dollars (US\$), in a commercial bank acceptable to the Bank. An initial authorized Designated Account (DA) ceiling of approximately US\$1.8 million will be established and could eventually be increased if justifiable by operational reasons. The minimum amount of each application with respect to direct payments by the Bank and reimbursements will be approximately 20% of the DA ceiling. LOA will establish the DA ceiling and minimum amount in the disbursement letter that will be discussed and confirmed with the Borrower during negotiations. Replenishment applications should be submitted by the Borrower ideally once a month but generally not later than once every four months, and may include reconciled bank statements as well as other appropriate supporting documents.

SOEs will be prepared on the basis of payments actually made through bank payment orders issued by Secretariat of Planning under instructions from the UGP. Bank orders reports will be drawn from the SIM system. SOE thresholds will be confirmed with procurement thresholds for consulting services and for goods and works.

Supervision of FM

During the first year, financial management supervision will take place at least twice a year and will include, among others, (a) reviewing of quarterly IFRs; (b) reviewing of the auditor's report and follow-up of issues raised by auditors in the management letter, as appropriate; (c) participation in project supervision, following up on any financial reporting and disbursement issues, (d) following up on internal control audit report, (e) following up on respective action plans. By the end of the mission, a financial management supervision report should be prepared, discussed with the borrowers and forwarded to the project team leader together with the ISR.

7. Procurement Arrangements

As part of the PDMI, Pelotas is responsible for implementing its respective project, the coordination of which will be done with support by a management unit (Unidade de Gestão do Projeto – UGP), located in an existing municipal structure (Secretariat of Planning). The UGP will plan, implement, supervise and monitor all procurement tasks carried out by the respective *Comissão de Licitação* under the project. In addition, the integrity of the programmatic approach will be guaranteed through the establishment of a high level coordination body and technical council comprising representatives of the all five municipalities as well as through the joint hiring of a Unidade de Articulação do Program (UAP).

Procurement for the PDMI that Pelotas will be carried out in accordance with the World Bank's "Guidelines: Procurement under IBRD Loans and IDA Credits", published in May 2004 and revised in October 2006; and "Guidelines: Selection and Employment of Consultants by World Bank Borrowers" published in May 2004 and revised in October 2006); and the provisions stipulated in the Loan Agreement. The general description of various items under different expenditure categories is described in the main PDMI PAD.

The overall risk assessment for the municipality of Pelotas is rated as high. Remedial actions have been identified in the attached Action Plan, and these were to be made effective in each municipality, independently of its risk range, to mitigate procurement risks. The measures to overcome these identified risks and which have been agreed are:

Table 11. Action Plan to Mitigate Procurement Risks

Activity No.	Action Plan	Time frame
1	Include in the PDMI Operations Manual the design of the entire procurement cycle and arrangements including clearances and approvals and description of the roles of all participant agencies. This document forms part of the Loan Agreement	Before appraisal.
2	(i) UGP to second or employ staff to work with procurement to work as procurement coordinator; (ii) UAP to hire an <i>ad hoc</i> procurement specialist experienced in Bank's financed projects to train, coordinate, monitor, and to proceed with quality control of the work carried out by UGP procurement coordinators in each participating municipality. The procurement specialist can be hired as an <i>ad hoc</i> consultant to work mainly on specific complex contracts or on a full-time basis.	Before effectiveness.
3	Purchase and/or make available equipment for the procurement staff of UGP, and <i>Comissões de Licitações</i> including: (a) computer equipment with internet access; (b) printer; (c) necessary software; (d) office furniture and file cabinets	Before negotiations
4	Provide an ample office space for the <i>Comissões de Licitações</i> and the procurement staff at the UGP, and a reserved area for the bidding opening ceremonies. The office spaces should consider the privacy that any bidding committee required.	Before effectiveness
5	Finalize the procurement plan for at least the first eighteen months of project implementation	Before negotiations
6	Develop/adapt a computerized procurement management system that shall be able to produce reports, including the procurement plan.	Before effectiveness
7	WB to train of UGP staff on Bank-procurement policies.	After effectiveness

Procurement Plan and Methods: Pelotas is preparing its procurement plan for the activities to be carried out during the first 18 months of project implementation. Upon completion, this plan will be approved by the Bank and filed in the project files, and will also be available in the PDMI database and in the Bank's external website. The procurement and consultant selection plans will be updated annually, and shall be submitted to the Bank in the first quarter of December of each year. The procurement plan should consist of: (i) goods, works and non-consulting services, including contract packaging, applicable procedures and process scheduling; and (ii) a consultant and training providers selection process plan for the projects' training and consultant services, including contract packaging, applicable procedures, and selection criteria. The municipality expressed its intention in engaging the *Universidade Federal de Pelotas*, and the *Universidade Católica de Pelotas* to undertake technical assistance and training activities.

During project preparation, the municipality expressed its intention in contracting the following entities to undertake technical assistance and training activities including: business administration, financial management, market strategies, quality control,

marketing, etc. Each case will be reviewed by the Bank upon receiving the respective justification as required by the procurement Guidelines:

- (i) *Fundação da Universidade Federal de Pelotas (UFP)*,
- (ii) *Fundação da Universidade Católica de Pelotas*;
- (iii) *Fundação da Pontifícia Universidade Católica de Pelotas (PUC-Pe)*;
- (iv) *Sociedade Educacional Noiva do Mar (SENM)*;
- (v) *Centro Federal de Educação Tecnológica de Pelotas (CEFET-Pe)* (to contract professors, technical staff and interns to provide technical assistance and capacity building to municipal staff of Pelotas, as well as, to hire students and trainees from these universities to support the municipality with project related activities in Pelotas;
- (vi) *Serviço Nacional de Aprendizagem Comercial (SENAC)*;
- (vii) *Serviço Brasileiro de Apoio às Micro e Pequenas Empresas (SEBRAE)*, and
- (viii) *Serviço Nacional de Aprendizagem da Indústria (SENAI)*.

Seemingly, Pelotas requested the sole sourcing under par. 3.9 (a) of Guidelines for *Banco do Nordeste do Brasil (BNB)* to support the start-up costs and initial operation of the micro-credit program (Crediamigo) in the municipality and the justification will be submitted to the Bank prior to signing the contract, as required by the Bank's Guidelines.

8. Environmental and Social Assessment

Institutional Framework

The Municipality of Pelotas is qualified by the State Environmental Authority, CONSEMA, to license activities with local impacts. The municipality has a Municipal Environmental Fund (FMMA) and a Council of Environmental Protection (COMPAM). The Municipal Secretary of Environmental Quality (SQA), created in 2001, is responsible for environmental protection, inspection and licensing, and oversees environmental licensing and inspection, according to the environmental legislation and guidelines established by COMPAM. Pelotas is working on a covenant with FEPAM to acquire further responsibilities over environmental licensing (beyond activities with strictly local impacts).

Environmental and Social Assessment

During project preparation it was agreed that the SQA staff and social workers of the housing department of the municipality would be responsible for evaluating and monitoring project investments with strictly local impacts and will work with state agencies in project investments with larger impacts. The SANEP will screen and monitor investments in the water and sanitation sector. The detailed screening of all first 18 month investments confirmed that the project investments in Pelotas will have strictly local impacts.

During project preparation, 53 road rehabilitation and/or paving projects were screened, none of which required widening of existing right-of-ways or the acquisition or displacement of people. The city is also proposing the rehabilitation of the Dom Antônio Zattera Park, landscaping and rehabilitation of park facilities and the Lobo da Costa

Street, which will become a pedestrian priority street. Two small bridges are included in the priority investments that will provide improved access to poor neighborhoods and will have localized impacts that are going to be mitigated through the application of the EMSF and specific construction guidelines.

Investments in road infrastructure will happen along existing right-of-ways not requiring any displacement of people. The main concern is with local access during construction and traffic safety issues during operation. The city is including sidewalk improvements and arborization programs in the proposed projects.

The Safety of Dams is being analyzed since the project includes water supply networks that will draw directly from two water reservoirs that will be used for water supply in the city. The results of this analysis will be reviewed by the Bank prior to any investment in WSS.

Pelotas is recovering a number of historical buildings with federal funds from the Monumenta Program. This program, with assistance from UNESCO, aims at recuperating and preserving historic building and ensures the original architecture is respected as required by Bank policies. Furthermore, the city has recently purchased an old shopping mall building that will become the new main Administrative Complex of the City. The building is a modern high-rise building in the downtown area that has been empty for a number of years. Under Component 1, the project will support works to improve the internal layout and infrastructure. These renovation projects are expected to have mostly localized impacts that can be mitigated through proper management and physical protection around the construction site.

Expansion of the Camelódromo – the existing market houses nearly 200 vendors and will be expanded for other street vendors. No land acquisition is necessary since the site is clear and currently used as a parking area for people coming to the Camelódromo and occasional events. The project will include alternative plans for parking and access to avoid conflicts with surrounding streets.

None of the proposed investments in the first 18 months in Pelotas requires economic or physical displacement of people nor are expected to negatively affect cultural property. The project's Resettlement Policy Framework applies to unforeseen economic or physical displacement of people and chance find guidelines for archeological and cultural artifacts are included in the EMSF.

The safeguard procedures are common for all municipalities. Prior to implementing projects that will draw existing dams for water supply purposes, the Municipality of Pelotas will have to inspect and evaluate the safety status of the existing dams and, if necessary, provide recommendations and remedial measures to improve safety of these dams.

Capacity Assessment

From the information provided and assessment during project preparation, the SQA, SANEP and social workers are among the most qualified to monitor and control the environmental and social aspects of the proposed investments in the project. During project implementation, special attention will be given in further strengthen integration of environmental and social aspects in planning and implementing infrastructure investments and strengthen citizen participation in the overall process.