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Report No: 82321-PE

INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT

PROJECT APPRAISAL DOCUMENT

ON A

PROPOSED LOAN

IN THE AMOUNT OF US\$35 MILLION

TO THE

REPUBLIC OF PERU

FOR THE

CUSCO REGIONAL DEVELOPMENT PROJECT

October 23, 2013

*Urban and Disaster Risk Management Unit
Sustainable Development Network*

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CURRENCY EQUIVALENTS

(Exchange Rate Effective August 8, 2013)

Currency Unit = Nuevos Soles Peruanos
S/.2.80 = US\$1
US\$0.36 = S/. 1

FISCAL YEAR

January 1 – December 31

ABBREVIATIONS AND ACRONYMS

COPESCO	Commission to Supervise the Cultural Tourism Plan PERU-UNESCO – <i>Comisión Especial para Supervigilar el Plan Turístico Cultural PERU-UNESCO</i>
CPS	Country Partnership Strategy
CRG	Cusco Regional Government
DBO	Design-build-operate
ESIA	Environmental and Social Impact Assessment
ESMF	Environmental and Social Management Framework
FM	Financial Management
GDP	Gross Domestic Product
IBRD	International Bank for Reconstruction and Development
ICB	International Competitive Bidding
IFC	International Finance Corporation
INEI	National Institute of Information and Statistics – Instituto Nacional de Estadística e Informática
MEF	Ministry of Economy and Finance – <i>Ministerio de la Economía y Finanzas</i>
METRA	Cusco Transport Improvement Project (P132505)
NCB	National Competitive Bidding
OGA	General Administrative Office of COPESCO – <i>Oficina General de Administración de COPESCO</i>
OM	Operations Manual
PCU	Project Coordination Unit
PDO	Project Development Objective
PER Plan COPESCO	Special Regional Project of Plan COPESCO – <i>Proyecto Especial Regional del Plan COPESCO</i>
PRRVV	Vilcanota Valley Rehabilitation and Management Project – <i>Proyecto de Rehabilitación y Gestión del Valle Vilcanota</i>
SIAF-MEP	Integrated Financial Management System- Project Implementation Module – Sistema Integrado de Administración Financiera – Módulo de Ejecución de Proyectos
SNIP	Peruvian National Public Investment System – <i>Sistema Nacional de Inversión Pública</i>
TORs	Terms of Reference

Regional Vice President:	Hasan A. Tuluy
Country Director:	Susan G. Goldmark
Sector Director:	Ede Jorge Ijjasz-Vasquez
Sector Manager:	Anna Wellenstein
Task Team Leader:	Zoe Trohanis

PERU
Cusco Regional Development Project

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PAD DATA SHEET*Peru**Cusco Regional Development (P117318)***PROJECT APPRAISAL DOCUMENT***LATIN AMERICA AND CARIBBEAN**Urban and Disaster Risk Management Unit*

Report No.: PAD575

Basic Information			
Project ID P117318	Lending Instrument Investment Project Financing	EA Category A - Full Assessment	Team Leader Zoe Elena Trohanis
Project Implementation Start Date 31-Jan-2014		Project Implementation End Date 31-Jan-2019	
Expected Effectiveness Date 31-Jan-2014		Expected Closing Date 31-Jan-2019	
Joint IFC No			
Sector Manager Anna Wellenstein	Sector Director Ede Jorge Ijjasz-Vasquez	Country Director Susan G. Goldmark	Regional Vice President Hasan A. Tuluy
Borrower: Republic of Peru			
Responsible Agency: Cusco Regional Government			
Contact: Helio Molina Telephone 51-581-540 No.:		Title: Executive Director PER Plan COPESCO Email: hmolina@copesco.gob.pe	
Project Financing Data(in USD Million)			
<input checked="" type="checkbox"/> Loan	<input type="checkbox"/> Grant	<input type="checkbox"/> Other	
<input type="checkbox"/> Credit	<input type="checkbox"/> Guarantee		
Total Project Cost:	52.10	Total Bank Financing:	35.00
Financing Gap:	0.00		
Financing Source		Amount	
Borrower		17.10	
International Bank for Reconstruction and		35.00	

Development									
Total							52.10		
Expected Disbursements (in USD Million)									
Fiscal Year	2014	2015	2016	2017	2018	2019	0000	0000	0000
Annual	2.00	9.00	10.00	12.00	1.00	1.00	0.00	0.00	0.00
Cumulative	2.00	11.00	21.00	33.00	34.00	35.00	0.00	0.00	0.00
Proposed Development Objective(s)									
To improve the quality of tourism and solid waste management services and increase the resilience of the tourism sector to the impacts of natural disasters in the provinces of Calca, Urubamba, and Cusco.									
Components									
Component Name						Cost (USD Millions)			
Development and Consolidation of Tourism Services						25.00			
Integrated Solid Waste Management						18.40			
Disaster Risk Management and Disaster Preparedness						2.60			
Institutional Strengthening, Management and Monitoring and Evaluation						6.10			
Institutional Data									
Sector Board									
Urban Development									
Sectors / Climate Change									
Sector (Maximum 5 and total % must equal 100)									
Major Sector		Sector		%	Adaptation Co-benefits %		Mitigation Co-benefits %		
Public Administration, Law, and Justice		Sub-national government administration		20					
Water, sanitation and flood protection		Solid waste management		30					
Water, sanitation and flood protection		Flood protection		20	20				
Industry and trade		General industry and trade sector		30					
Total				100					
<input type="checkbox"/> I certify that there is no Adaptation and Mitigation Climate Change Co-benefits information applicable to this project.									
Themes									

Theme (Maximum 5 and total % must equal 100)		
Major theme	Theme	%
Social protection and risk management	Natural disaster management	25
Urban development	City-wide Infrastructure and Service Delivery	30
Urban development	Cultural Heritage	35
Environment and natural resources management	Pollution management and environmental health	10
Total		100

Compliance		
Policy		
Does the project depart from the CAS in content or in other significant respects?	Yes []	No [X]
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 [X]
Does the project meet the Regional criteria for readiness for implementation?	Yes [X]	No []

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

Legal Covenants			
Name	Recurrent	Due Date	Frequency
Project Coordination Committee		31-Dec-2013	

Description of Covenant
Schedule 2, Section I, B, 1 (a): The Borrower shall cause the Region of Cusco, acting through PER Plan COPESCO, to establish by no later than December 31, 2013, and thereafter operate and maintain throughout the period of implementation of Project activities, a Project Coordination Committee.

Name	Recurrent	Due Date	Frequency
Technical Working Groups		31-Dec-2013	
Description of Covenant			
Schedule 2, Section I, B, 1 (b): The Borrower shall cause the Region of Cusco, acting through PER Plan COPESCO, to establish by no later than December 31, 2013, and thereafter operate and maintain throughout the period of implementation of Project activities, three Technical Working Groups, one for each of Components 1, 2 and 3 of the Project.			
Conditions			
Name			Type
Execution of Subsidiary Agreement			Effectiveness
Description of Condition			
Article V, 5.01 (a): The Subsidiary Agreement has been executed on behalf of the Borrower and the Region of Cusco			
Name			Type
Adoption of the Operations Manual			Effectiveness
Description of Condition			
Article V, 5.01 (b): PER Plan COPESCO has prepared and adopted the Project Operations Manual in a manner acceptable to the Bank			
Name			Type
Implementation of the Tourism Competitive Fund (Disbursement Category 2)			Disbursement
Description of Condition			
Schedule 2, Section IV, B, 1 (b): No withdrawal shall be made under Category (2) unless and until, the PER Plan COPESCO has prepared and adopted an CF Implementation Manual for the pilot competitive fund (<i>fondo concursable</i>) in a manner and substance satisfactory to the Bank.			
Team Composition			
Bank Staff			
Name	Title	Specialization	Unit
John Morton	Senior Urban Environment Specialist	Senior Urban Environment Specialist	LCSDU
Ellen Hamilton	Lead Urban Specialist	Lead Urban Specialist	UDRUR
Patricia M. Acevedo	Program Assistant	Program Assistant	LCSDU
Zoe Elena Trohanis	Sr Urban Spec.	Sr Urban Spec.	LCSDU
Jose Vicente Zevallos	Senior Social Development Specialist	Senior Social Development Specialist	LCSSO
Mariana Margarita Montiel	Senior Counsel	Senior Counsel	LEGLE
Ana Lucia Jimenez Nieto	Financial Management Specialist	Financial Management Specialist	LCSFM

Jean-Jacques Verdeaux	Senior Procurement Specialist	Senior Procurement Specialist	LCSPT		
Martin M. Serrano	Senior Counsel	Senior Counsel	LEGES		
Raquel Almeida Campos	Temporary	Temporary	LCSDU		
Elizabeth Huaman Carnero	Team Assistant	Team Assistant	LCC6C		
Daniel Mira-Salama	Environmental Specialist	Environmental Specialist	LCSEN		
Jose Yukio Rasmussen Kuroiwa	Procurement Specialist	Procurement Specialist	LCSPT		
Marco Antonio Joaquin Rodriguez Corrales	Senior Disaster Risk Management Specialist	Senior Disaster Risk Management Specialist	LCSDU		
Robert H. Montgomery	Lead Environment Specialist	Lead Environment Specialist	LCSEN		
Monica Joyce McDonough	Junior Professional Associate	Junior Professional Associate	LCSDU		
German Nicolas Freire	Social Development Specialist	Social Development Specialist	LCSSO		
Omar Guido Concepcion Yanac	E T Consultant	E T Consultant	LCSDU		
Rafael Antonio Corral Coronel	Temporary	Temporary	LCSEG		
Non Bank Staff					
Name	Title	Office Phone	City		
Locations					
Country	First Administrative Division	Location	Planned	Actual	Comments
Peru	Cusco	Cusco	X		

I. STRATEGIC CONTEXT

A. Country Context

1. Peru has enjoyed a period of broad-based rapid economic growth. Sound macroeconomic management during the boom years created the fiscal space needed for countercyclical policies to soften the impact of the global economic crisis. Despite the magnitude of the challenges generated by the global economic crisis, financial and exchange rate stability was preserved. Economic growth decelerated sharply in 2009, but remained positive, as external demand and an anti-cyclical public spending program propped up growth. A two-year economic stimulus plan was launched in 2009 amounting to US\$4.9 billion, or about 3.5 percent of gross domestic product (GDP). The plan focused primarily on increased public expenditures and attempted to balance the need for a stimulus in the short term while also reflecting medium-term priorities. Infrastructure projects accounted for approximately US\$2.4 billion, around 51 percent of planned expenditures, out of which US\$912 million were earmarked for infrastructure projects to be selected and implemented by regional governments. As with any stimulus plan, the challenges included: (i) ensuring the effective implementation of these investments, especially at the subnational level; and (ii) ensuring that these investments promote economic activity in a socially and environmentally sustainable way.

2. Growth has been resilient despite the recent global economic crisis. Economic activity has recovered since 2009 after rebounding sharply in 2010 to 8.8 percent. In 2011, GDP grew at a rate close to 7 percent, led by strong domestic demand and in 2012, despite the weak macroeconomic external environment, GDP expanded by 6.3 percent. The main contributors to GDP growth were private investment and private consumption that grew by 13.6 percent and 5.8 percent, respectively. In 2012, economic activity expanded on the back of investment dynamism. Private investment was driven by positive entrepreneurial expectations and an expansion in the construction sector. Public investment recovered and increased by 20.9 percent, driven by the fiscal stimulus plan. Based on the 2008-2009 experience, in 2011 the Ministry of Economy and Finance (MEF) launched a “preemptive” Stimulus Plan, designed to support the economy in the continued external uncertainty. This Stimulus Plan was implemented in two tranches. The first was launched in November-October 2011 and totaled about US\$900 million (2.5 billion *nuevos soles*, or 0.6 percent of GDP). This tranche’s main objective was to revive public spending as execution declined when the new Government took office in 2011.

3. Fast economic growth has been accompanied by growth in employment and incomes yielding an important decline in poverty rates. Poverty fell from 55.6 percent to 27.8 percent between 2005 and 2011, while extreme poverty was reduced from 15.8 percent to 6.3 percent. The continued reduction in poverty is remarkable, given that 2008 saw high food price inflation and the 2009 economic slow-down due to the global economic crisis. However, poverty incidence remains unequal in geographic terms, with the rural poverty rate above 50 percent. While inequality of opportunity remains high, Peru has made substantial progress in addressing it, supported by increased public investments in infrastructure, water, sanitation and electricity in recent years. Despite this progress, large gaps remain in terms of the demand for and quality of

infrastructure investment, as reflected by the fact that Peru ranked 19th out of 23 Latin American and Caribbean countries in a 2008 infrastructure ranking.¹

4. Peru's strong economic performance over the past decade has been accompanied by a significant shift in public expenditure authority and resources to the subnational level. Until 2002, Peru was one of the more centralized countries in Latin America, with only 12 percent of its public expenditures managed by subnational governments.² A policy shift that year led to the passage of the Decentralization Framework Law³, which established the guiding principles of a political and fiscal decentralization process which has since made significant strides. A new autonomous level of regional governments was formally created in 2002, to complement the existing Provincial and municipal District governments at the local level. As part of the decentralization process, more responsibilities, functions and resources have been transferred from the central government to subnational governments. These measures have been accompanied by mechanisms to ensure efficient use of these resources and an adequate provision of public services at the subnational level. Accordingly, the non-financial expenditure of the subnational governments increased from 34 percent of non-financial general government expenditure in 2004 to 38 percent in 2011. Likewise, the share of subnational governments in public investment increased from 44 percent in 2004 to 58 percent in 2011.⁴ However, there are ongoing significant challenges in the decentralization process, related to allocation of resources from mining revenues and the local capacity for implementing the public investment programs.⁵

B. Sectoral and Institutional Context

5. Tourism in Peru has been growing steadily. Between 2002 and 2012, international tourist arrivals grew from 1.1 to 2.8 million foreign visitors while foreign exchange earnings quadrupled from US\$837,000 to US\$3.288 million. In 2012, tourism generated 1,081,035 jobs and directly contributed 3.7 percent to national GDP. It is estimated that by 2021, 5.1 million foreign tourists will visit Peru and foreign exchange earnings will have increased to US\$6.852 million, with about 1.274 million employed in the tourism sector. Tourism will contribute more to national GDP in the future and is expected to comprise 4.24 percent of GDP in 2021. The growth potential of the tourism sector is high, both in international and in domestic tourism. The number of international tourists is growing at 8.1 percent per year, which is well above the Latin American average of 3.7 percent and the world average of 2.2 percent. Additionally, the increased purchasing power of the middle class in Peru has also contributed to the considerable increase in domestic leisure travelers.

6. Due to its historic and cultural heritage, the Cusco Region is one of the most visited tourist destinations in South America and is the principal tourist destination in Peru, accommodating 88 percent of the country's international visitors. Over the last 10 years, the number of tourist

¹Ranking de Infraestructura 2008, Anand Hemmani, CG/LA.

²Compared to an average of 20 percent for Latin America as a whole and 26 percent for the OECD countries during the same period.

³Law No. 26922, October 16, 2001

⁴Ministry of Economy and Finance, 2012. Multi-Annual Macroeconomic Framework (Marco Macroeconómico Multianual) 2013-2015.

⁵World Bank. 2010. Peru: The Decentralization Process and its Links with Public Expenditure Efficiency. Washington, DC. <https://openknowledge.worldbank.org/handle/10986/12894>

arrivals has grown more than two and a half times to over 2.8 million per year, growth that has not been matched by an equivalent improvement in the provision of tourism services.⁶ Additionally, the Region of Cusco is important in terms of trade and industrial production. However, despite the region's high potential for development, its human development index indicators are below the national average.⁷

7. The Cusco Regional Government (CRG) developed the 2021 Cusco Strategic Development Plan (*Plan Estratégico de Desarrollo Regional Concertado, Cusco a 2021*)⁸, which outlines the goal of continued development of the region in a way that adequately accounts for its unique social, cultural and environmental values. The plan specifically proposes investments in infrastructure that would accommodate the ongoing growth of the tourism sector with adequate consideration for environmental concerns and disaster risk mitigation. Responding to this regional strategy, the following key sectoral strategies have been developed:

(a) *Development of tourism activities:* The Regional Strategic Plan for Tourism (*Plan Q'ente*) promotes the development of tourist activities in the region with social, cultural and environmental responsibility as well as the consolidation of the Cusco region as a nationally and internationally competitive tourism destination, promoting local investment initiatives. The CRG is committed to the management, conservation and preservation of archeological, cultural and natural patrimony with the participation of the local population, the Government and the private sector.

(b) *Environmental Management:* The Institute for the Management of Water and the Environment (*Instituto de Manejo de Agua y Medio Ambiente*) has adopted a regional strategy that supports institutional development, watershed management, management of natural resources, development of coordination and dialogue, capacity development and awareness and adaptation and mitigation of climate change. Among the activities to be promoted is the planning of integrated management of solid waste which was supported under the World Bank-financed Vilcanota Valley Rehabilitation and Management Project (PRRVV)⁹. The management, collection and disposal of solid waste is a critical issue in the provinces of Cusco, Calca and Urubamba, which form important parts of the tourism circuit in the Sacred Valley.

(c) *Natural Disasters:* The Regional Disaster Prevention and Reduction Plan (*Plan Regional de Prevención y Atención a los Desastres de la Región Cusco*) outlines the vision and actions for the management of natural disaster risk and prevention in the region including improved risk estimation, monitoring and information, undertaking activities to prevent and reduce risks; mainstreaming risk prevention in planning, improving community participation in the prevention of disasters and optimizing the response to disasters. The tourism industry and the associated infrastructure, including Machu Picchu Pueblo, are highlighted as economically important zones that are vulnerable to natural disasters. In 2010, severe flooding affected the Sacred Valley,

⁶Ministry of Culture statistics, January 2002-December 2012, <http://www.mincetur.gob.pe>

⁷INEI, Censo Nacional de Población y Vivienda, 2011.

⁸<http://www.arariwa.org.pe/CIG-0005.pdf>

⁹P082625, closed on June 30, 2011.

causing nearly US\$240 million in damage to infrastructure and the agriculture sector and washing out the only railway line to reach Machu Picchu. This event left over 3,000 tourists stranded in Aguas Calientes (the access point for the ruins). The estimated losses to the tourist industry were estimated at US\$1 million a day for each day the access was cut off. The CRG estimated that 15,000 people in the tourism business were unemployed for several months.

8. To mobilize financing for these key aspects of the Cusco Strategic Development Plan in an integrated way, the CRG has elaborated the Public Investment Program¹⁰ “Consolidation and Diversification of the Tourism Product – Sacred Valley of the Incas among the Provinces of Cusco, Calca and Urubamba in the Cusco Region (*Programa de Inversión Pública “Consolidación y Diversificación del Producto Turístico – Valle Sagrado de los Incas entre las Provincias de Cusco, Calca y Urubamba de la Región Cusco”*), which is being developed through the public investment process of the Government of Peru. The Program amounts to S/.206.7million (US\$73.8million) and consists of four major components: (a) Entrepreneurial Competitiveness comprised of a pilot competitive fund for micro and small enterprises to enhance their ability to access the tourism market; (b) Consolidation of “Classic” Tourist Attractions and Diversification of Tourism Offerings, Integrated Solid Waste Management and Disaster Risk Management; (c) Technical Assistance for the Coordination of Public-Private Partnerships and Commercialization of Tourism Services and (d) Program Management and Monitoring.

9. The proposed Project will finance key elements of this Program, with the exception of investments in diversification of new tourism sites. The reason for excluding this component from the Project is due to the high level of complexity in supporting the archeological investigation required to open up new sites for increased access to tourists. This process would involve the Ministry of Culture’s oversight, require high levels of force account, and would take much longer than the five year timeframe of the proposed Project. The CRG has agreed to finance this component with a separate source of funds. Though it is not included in the Bank-financed Project, the diversification component remains in the overall Program to be implemented by the CRG and will be executed by the same coordination unit as the rest of the Bank-financed Project, ensuring the coherence of investments.

10. In addition to the proposed Project, the CRG is preparing the Cusco Transport Improvement Project (P132505, also known as “METRA”) to upgrade the main expressway in Cusco city with World Bank financing. The total project cost is approximately US\$130 million and is expected to be presented to the World Bank’s Board of Directors in March 2014.

11. The CRG has started a modernization process aimed at improving its efficiency and achieving long term sustainable development. The CRG underwent a credit rating assessment in

¹⁰ In Peru, the Ministry of Economy and Finance uses the National Public Investment System (*Sistema Nacional de Inversión Pública*, or SNIP) to manage national and subnational public investment projects (Proyectos de Inversión Pública, or PIPs). The SNIP establishes a project cycle that includes pre-investment, investment and post-investment phases that all PIPs must follow. This Project is categorized as a “Program” in the SNIP system, composed of several PIPs that make up the Project’s components.

2011¹¹ to expand its financing options and facilitate its access to financial markets. The work related to the credit rating was expanded on in 2013 with a financial capacity assessment designed to assess the CRG's ability to incur loan and counterpart obligations in connection with the proposed Project and METRA. The objective of the financial capacity assessment was to base decisions on the size of the two projects as well as the counterpart and loan proportions of the two projects on a forward-looking assessment of resources available vis-à-vis current investment commitments while considering investment needs of the other nine provinces in the region not covered by these operations.

12. In alignment with the World Bank Group strategy, the proposed Project will be the first International Bank of Reconstruction and Development (IBRD)-financed investment operation to be prepared and implemented by a regional government in Peru. The proposed operation builds on the longstanding relationship between Peru and the Bank, including the Peru Rural Roads Program (PCR), which was initiated in 1995 and scaled up from a focus on the poorest 12 departments to subsequent phases covering the entire country. The PCR integrated community participation in a large-scale rural roads program with best practices in terms of flexibility and adaptability in project implementation, increased ownership, and efficient management of road assets.¹²

13. The proposed operation is directly linked to the work already begun under the PRRVV (approved in 2004) to enhance the CRG's capacity to identify, prepare, and implement infrastructure investments at the regional level. The PRRVV supported the preparation of the proposed solid waste management component as well as studies and capacity building with local governments that are being built upon in the proposed disaster risk management component. The proposed operation incorporates lessons learned during the design and implementation of PRRVV and the CRG will benefit from PER Plan COPESCO's (Special Regional Project of Plan COPESCO, or *Proyecto Especial Regional Plan COPESCO*, hereafter referred to as COPESCO) experience in implementing World Bank funded Projects. COPESCO is the CRG's implementation agency focused on improving the quality of life of its citizens through investments in tourism and basic infrastructure.¹³

14. The International Finance Corporation (IFC) is currently preparing advisory services on "Improving the Investment Climate for Tourism in Peru," focused on streamlining the procedures related to opening and operating a tourism business in the Cusco Region, such as lodging establishments, restaurants, tourism and travel agencies. This work by the IFC is complementary to the proposed Bank-financed Project, as the advisory services will build private sector capacity and improve the business environment in the tourism sector, while the Bank-

¹¹The credit rating assessment, funded by the Public-Private Infrastructure Advisory Facility's Sub-National Technical Assistance (PPIAF-SNTA) with support from the IFC, established the CRG's capacity to meet its financial commitments, resulting in a BBB- risk rating for long term debt. The credit rating assessment concluded that the CRG is a stable institution with a growing income generation capacity; however, it needs to strengthen its investment rates and expenditures execution.

¹²The PCR's positive impacts on rural transport, local economic development and local governance in Peru earned it the World Bank's President's Award for Excellence in 2001.

¹³COPESCO was founded in 1969 as a joint initiative between UNESCO and the Government of Peru for the preservation and enhancement of the historical, cultural and ecological assets of the Cusco Region and in particular, the Vilcanota Valley, originally the Special Commission to Supervise the Cultural Tourism Plan PERU-UNESCO.

financed project will focus on enhancing the quality and resilience of tourism-related infrastructure and public services.

C. Higher Level Objectives to which the Project Contributes

15. The Project is consistent with the FY12-FY16 Peru Country Partnership Strategy (CPS, Report No. 66187-PE), discussed by the Executive Directors on February 1, 2012. The proposed operation is fully aligned with the CPS, supporting three of its four strategic objectives: (i) connecting the poor to services and markets; (ii) sustainable growth and productivity; and (iii) improved public sector performance for greater inclusion. The CPS also focuses on supporting subnational investments and capacity building in public management as well as on the implementation of delegated sectoral functions. The proposed Project will thus support the Bank's broader mission to end extreme poverty and promote shared prosperity, particularly through activities providing technical assistance to local small and micro enterprises providing tourism-related goods and services, targeted in the rural areas of the Sacred Valley where poverty and inequality are highest. The Project also supports these goals by improving the delivery of solid waste services and includes a Social Inclusion Plan to formalize waste pickers by providing employment opportunities related to recycling activities. Improvements in infrastructure to better withstand floods and landslides and the installment of early warning systems will increase resilience to disasters and protect vulnerable populations and tourists in the region. This Project is also directly aligned with the 2021 Cusco Strategic Development Plan, as explained above in section B.

II. PROJECT DEVELOPMENT OBJECTIVES (PDO)

A. PDO

16. The Project Development Objective is to improve the quality of tourism and solid waste management services and increase the resilience of the tourism sector to the impacts of natural disasters in the provinces of Calca, Urubamba, and Cusco. This will be accomplished by improving the development and consolidation of tourism services, enhancing capacity for solid waste management, and scaling up disaster risk management efforts in the provinces of Calca, Urubamba, and Cusco, which makes up the Sacred Valley and surrounding tourism circuits in the Cusco region.

Project Beneficiaries

17. The target Project beneficiaries are comprised of approximately 1,146,719 people, distributed throughout the provinces of Cusco (population 427,580), Calca (population 72,583) and Urubamba (population 63,039) and an estimated 688,644 annual tourists in the Project area. The target population was identified considering the residents and tourists who are directly or indirectly involved in touristic activities and who will benefit from improved solid waste management services as well as from the area's increased resilience to natural disasters.

PDO Level Results Indicators

18. The progress towards achieving the PDO will be monitored by the following indicators:

- (a) Percent reduction in the dissatisfaction rating of the upgraded tourism sites under the Project;
- (b) Direct Project beneficiaries (percentage of which are female);
- (c) Number of people (tourists and residents) in the Project area from whom waste is collected and disposed in one of the Project sanitary landfills; and
- (d) Number of people (tourists and residents) covered by a functioning early warning system for natural disasters under the Project.

III. PROJECT DESCRIPTION

A. Project Components

19. The Project consists of four components:

20. *Component 1: Development and Consolidation of Tourism Services (US\$25 million, of which US\$18.8 million is Bank-financed).* The objective of this component is to improve the quality and coverage of tourism services in the Sacred Valley and surrounding areas. The component includes:

(1) Consolidating classic tourist attractions in the Sacred Valley by improving and expanding existing infrastructure through the provision, improvement and/or construction of, *inter alia*: access ways to touristic sites; internal trails (including footpath surfaces, staircases, bridges and railings); internal signage (both informative and interpretive); traffic distribution points; lighting; drainage; touristic centers; toilets; ticketing offices; parking lots; craft markets; and other small ancillary infrastructure in touristic sites.

(2) Developing and implementing a pilot competitive fund (*fondo concursable*) to provide technical assistance to private small and micro enterprises in order to improve the competitiveness of touristic products and services.

(3) Strengthening the institutional capacity of agencies and institutions involved in the operation of touristic activities in the Sacred Valley, in order to: (i) commercialize and position touristic products and services in the domestic and international markets; (ii) collect touristic related data and prepare a database for the evaluation and analysis of the development of the sector.

21. *Component 2: Integrated Solid Waste Management (US\$18.4 million, of which US\$13.8 million is Bank-financed).* This component aims at improving the local capacity to clean streets and public places and to efficiently collect, transport and dispose of solid waste in the Provinces of Calca, Urubamba and Cusco through, *inter alia*: (i) the construction of three (3) new landfills, one in each of the Provinces of Calca, Urubamba and Cusco; (ii) the strengthening of provincial and municipal administrations' institutional capacity to administer the management of solid waste facilities and services; (iii) investments in solid waste services at the district level to improve collection, recycling, and cleaning of streets and public spaces; and (iv) carrying out of communication campaigns in local communities for the promotion of adequate waste management practices and environmental education.

22. *Component 3: Disaster Risk Management and Disaster Preparedness (US\$2.6 million, of which US\$1.9 million is Bank-financed).* The objective of this component is to increase the resilience of the local population, tourists, and infrastructure in touristic areas with high vulnerability to natural disasters. The component is aimed at increasing the resilience of the local population and tourism infrastructure to natural disasters through, *inter alia*: (i) designing and implementing early warning systems to anticipate the flooding of the Vilcanota and Patacancha rivers in the Sacred Valley and Ollantaytambo; (ii) designing and implementing an integrated approach to the reduction of geological and climatic risks in the micro-basin of K'itamayu river in Písaq; (iii) designing and implementing an integrated approach to mitigate external geodynamic risks in the Ccochoq river basin in the Province of Calca; and (iv) updating the disaster risk management plan for the Sacred Valley, including plans for the evacuation of tourists, and carrying out evacuation training and simulation exercises with the local population and tourists.

23. *Component 4: Institutional Strengthening, Management and Monitoring and Evaluation (US\$6.1 million, of which US\$0.5 million is Bank-financed).* This component will support the capacity building of the principal institutions involved in the operation of tourism activities in the Sacred Valley, and COPESCO, including its Project Coordination Unit (PCU). The component would strengthen the institutional capacity of the PCU, PER Plan COPESCO, to enhance the institutional capabilities required for the successful implementation of Project activities, including compliance with procurement, safeguards, financial management, and monitoring and evaluation requirements.

24. Greater detail on Project components and activities is provided in Annex 2.

B. Project Financing

25. The selected lending instrument is Investment Project Financing. The loan will be to MEF, which will on-lend the proceeds with the same terms and conditions to the CRG. The CRG will repay the loan proceeds by authorizing an intercept on central government transfers. This transfer mechanism for repayment was developed and implemented successfully under the PPRRV project.

Project Cost and Financing

26. The Project cost will be US\$52.1 million, of which US\$35 million would be financed by the IBRD.

Project Components	Project cost (US\$ millions)	IBRD Financing (US\$ millions)	% Financing
1. Development and Consolidation of Tourism Services	25.0	18.8	75
2. Integrated Solid Waste Management	18.4	13.8	75
3. Disaster Risk Management and Disaster Preparedness	2.6	1.9	75
4. Institutional Strengthening, Management and Monitoring and Evaluation	6.1	0.5	8
Total Costs	52.1	35.0	67

Total Project Costs	52.1	35.0	67
Front-End Fees	0.1	-	0
Total Financing Required	52.2	35.0	67

C. Lessons Learned and Reflected in the Project Design

27. The Project was designed based on the knowledge and experience gathered from the PRRVV and other Bank-financed projects in the tourism, solid waste management, and disaster risk management sectors.

28. Main lessons from the PRRVV include:

(a) *Project design should be simple with a well-focused PDO supported by a limited number of activities that should have strong synergies, especially for small projects.* The PRRVV attempted to address a broad range of multi-sectoral issues ranging from cultural heritage preservation to regional development and provision of basic infrastructure services. Addressing this complex range of themes required multiple institutions and large teams on both the Bank and the Government side. The proposed Project is larger in scope, but builds on previous experience and has an appropriate amount of capacity strengthening activities and technical assistance.

(b) *Centralized implementation arrangements are inappropriate for a decentralizing country where Project activities are concentrated in one area.* The location of the original PRRVV PCU in Lima required an expensive and time consuming restructuring process. The proposed Project's PCU is housed within COPESCO under the GRC.

(c) *Participatory processes during Project preparation will not substitute for efficient inter-institutional coordination mechanisms.* Some activities required coordination among several institutions at different government levels, such as the revisions and approvals of the feasibility studies. Poor inter-institutional coordination and communication created delays and often resulted in contradictory messages. An institutional assessment has been carried out to consider all institutions involved in the preparation and implementation of the Project. An inter-institutional Coordination Committee will ensure clear lines of communication among project stakeholders.

29. Lessons from other Bank-financed projects in the tourism, solid waste and disaster risk management sectors include:

(a) *Maximizing the value of existing cultural assets to benefit local economic development.* Maximizing linkages between existing cultural heritage sites and poverty reduction through income generation, employment opportunities, and empowerment of local communities is essential for local sustainable development. The proposed Project has incorporated technical assistance to small and microenterprises in the tourism sector as well as to support the commercialization and positioning of tourism services domestically and internationally.

(b) *Solid waste management systems require integrated approaches.* Early during Project implementation, it is important to establish the institutional structures required to

sustain project activities. Financial sustainability is crucial to project success and can be achieved by linking service improvements to higher payment rates. The proposed Project has established a sustainable model for payment for solid waste services through a fiscal intercept mechanism agreed to by local governments. The Project has also included monitoring and evaluation to establish the service baseline and measure improvements.

(c) *Natural disaster losses are on the rise as people and assets tend to concentrate in areas prone to natural hazards*¹⁴. As both tourists and tourism assets in Cusco are vulnerable to disasters, a proposed component will focus on reducing vulnerability.

IV. IMPLEMENTATION

A. Institutional and Implementation Arrangements

30. The CRG will have overall responsibility for the Project, with COPESCO serving as the implementing agency. An institutional assessment of COPESCO has been carried out and used to determine staffing and organizational arrangements for the Project.

31. *Implementing Agency.* COPESCO is the implementation agency and has established a PCU that will be responsible for overall implementation and will coordinate the actors involved in the Project's execution. This unit within COPESCO builds on the previous capacity built through the PRRVV to ensure an adequate implementation pace and to allow for accountability. The PCU will be responsible for implementation of all Project activities, internal and external communications, financial management, procurement and compliance with safeguards and will be strengthened as needed with additional staff and consultants to ensure adequate capacity.

32. *Project Coordination Committee.* This committee will be established by the GRC in order to provide high level coordination of the Project and ensure Project alignment with broad strategic objectives. The Committee will include representatives from the key government institutions and civil society stakeholders, for example, representatives from MEF, the CRG, the three participating Provinces (Cusco, Calca and Urubamba), and other stakeholders. The Terms of Reference (TORs) for the Committee, including the membership and meeting frequency, are included in the Operations Manual (OM), to be adopted prior to effectiveness of the Project's Loan Agreement. Greater detail on the Project's implementation arrangements is provided in Annex 3. The Project's Implementation Support Plan can be found in Annex 5.

B. Results Monitoring and Evaluation

33. The results framework has been developed in close coordination with COPESCO. The PCU will consolidate the data at the project level and produce semi-annual reports to monitor progress. Overall responsibility for monitoring and evaluation of the Project will lie with COPESCO, which will provide timely information about the Project's implementation progress, including qualitative information on the execution of selected activities, procurement and contractual decisions, accounting and financial recording, and other operational and administrative matters. The Project's OM will provide specific details regarding monitoring and

¹⁴The Bank's Global Facility for Disaster Reduction and Recovery (GFDRR) has conducted various studies demonstrating the rising economic losses due to disasters on a global scale.

evaluation responsibilities. Additional detail on the Project’s results monitoring and evaluation framework can be found in Annex 1.

C. Sustainability

34. All activities funded by the Project are priority investments identified by the CRG according to their 2021 Cusco Strategic Development Plan and other key sector plans. All investments proposed under the Project are included in the Public Investment Program “Consolidation and Diversification of the Tourism Product – Sacred Valley of the Incas among the Provinces of Cusco, Calca and Urubamba in the Cusco Region.” This Program has undergone a rigorous internal vetting process required by the Government of Peru through the National Public Investment System (*El Sistema Nacional de Inversión Pública*, or SNIP) including government approval of feasibility studies and preliminary designs, followed by a process declaring the viability of all subcomponents and activities, explicitly addressing operating and maintenance costs.

35. Each of the tourism investments has undergone a financial and institutional analysis to ensure sustainability. Principal entities, such as the municipalities and/or the Department of Culture, have signed agreements confirming that they will provide adequate funding for the operation and maintenance of improved assets. Assessments of the fees that will be charged to support the operation and maintenance costs have been carried out for each subcomponent during their preparation to inform the municipalities and counterparts of the appropriate fee levels for each site.

36. Solid waste services in the Latin American region typically are financed through a combination of tariffs and fees and other sources including general revenues or cross subsidies from other basic services. Cost recovery through fees and tariffs charged to consumers, although beneficial, has not been shown to be a prerequisite to cover the costs of the system and ensure adequate quality and sustainability. The Project, through studies being undertaken by COPESCO, is finalizing a two pronged strategy to both (i) increase cost recovery during the period of the project and promote mechanisms that would help improve cost recovery over the longer term, and (ii) provide a guarantee for operation and maintenance costs in the short, medium and long term. Cost recovery options for collection and disposal are under review by COPESCO and MEF, with support from the Bank. Based on this assessment, the Project will include institutional strengthening to develop and improve these cost recovery options in the Provinces and municipal Districts.

V. KEY RISKS AND MITIGATION MEASURES

A. Risk Ratings Summary Table

Risk Category	Rating
Stakeholder Risk	Moderate
Implementing Agency Risk	High
- Capacity	High
- Governance	Moderate

Project Risk	High
- Design	High
- Social and Environmental	High
- Program and Donor	Low
- Delivery Monitoring and Sustainability	High
Overall Implementation Risk	High

B. Overall Risk Rating Explanation

37. The overall level of risk for the financed activities has been assessed as high. The main risks identified are:

(a) *Sustainability Risk*: Given the amount of counterpart funding linked to the Project, there is the risk that the Government might not provide adequate counterpart funding in later years due to the political cycle (with elections approaching in 2014) and potential changes in investment priorities of a new administration. This risk is managed, however, as the counterpart funds and agreements included in the Project's Loan Agreement are obligatory for incoming administrations to comply with and finance.

(b) *Social Risks*: The proposed Project investments and works, while not in the immediate area or adversely affecting World Heritage Sites, will be implemented in a highly sensitive social and cultural heritage context. However, the Project presents a significant opportunity through its high development impact potential. The mitigation strategy for social risks of the Project builds upon the experience in the PRRVV and includes: (i) technical designs that minimize potential environmental and social impacts and risks; (ii) technically strong social and environmental staff; (iii) training programs to build capacity among social and environmental staff; (iv) a robust consultation process for each subcomponent; (v) a communication strategy to build broad community support concerning the location of the new solid waste disposal sites; and (vii) the establishment of effective grievance redressal mechanisms.

(c) *Implementation Capacity*: Project implementation may be affected if COPESCO is unable to attract new staff to supplement its existing administrative and human resource capacity. To counter this risk the Bank has agreed with COPESCO on a staffing plan and budget that includes technical assistance and terms of reference for key personnel.

(d) *Political Risk*: The proposed Project has garnered the support of the President of the CRG as well as the mayors of the municipalities participating in the Project. However, with elections for the CRG in 2014, it is possible that human resources could shift during the election period, the Project could be framed in the context of negative campaigning, and if the political leadership changes, priorities could shift to other development issues. This risk is being mitigated through broad consultation with a range of stakeholders at the regional and municipal level to ensure ownership and sustainability of investments

beyond the political cycle and phasing the investments to help ensure the Project benefits will be evident both before and after the election period.

(e) *Reputational Risk*: There is the potential for reputational risk for the Bank due to the proposed Project's high visibility and its historical and cultural significance given the geographic focus on the Sacred Valley and the Municipality of Cusco, which is a UNESCO (United Nations Educational, Scientific and Cultural Organization) World Heritage Site and the entry city to Machu Picchu. There exists some risk that the Province of Cusco may fail to adequately close the existing Cusco waste dump, which has not been properly managed. Such failures could harm vulnerable communities living in close proximity to the dump. Peruvian legislation requires that an adequate closure plan be developed and implemented, with closure occurring once the new Cusco landfill is constructed. The Project will provide technical assistance to the Province of Cusco to support dump closure and will support economic development and delivery of basic services in communities near the existing dump and the new landfill as part of the Project safeguards instruments.

38. Additional information on the Project's risks can be found in Annex 4.

VI. APPRAISAL SUMMARY

A. Economic and Financial Analysis

39. The influx of tourists in the Sacred Valley and the resulting economic and social benefits are expected to continue to rise as a result of the proposed Project. The Government's strategy supports expanding infrastructure and improving competitiveness to enhance tourism services and better integrate local value chains to maximize direct and indirect benefits. The Government expects to upgrade tourism attractions and services to increase the number of tourists who visit, their length of stay, and their spending. As a result, tourists' satisfaction and local residents' wellbeing would increase.

40. Based on simulations run in studies of the potential benefits of the Project, the proposed intervention will, by conservative estimates, yield an increased effective demand of over 180,000 new tourists in 2020 that wouldn't have visited without the intervention. Such figures will likely increase to more than 582,000 total new tourists in 2026. These visitors will likely spend twice as much time in the Sacred Valley than they currently do. Under a moderate scenario, private profits will increase from annual net benefits (flows) in the order of almost 27 million *nuevos soles* (US\$9.7 million) in 2017 to 309 million *nuevos soles* (US\$111 million) in 2027. Under moderate estimates, the net benefit of implementation would yield an internal rate of return of 28 percent, easily exceeding the discount rate of 9 percent, and would yield a net present value (NPV) of over 626 million *nuevos soles* (US\$225 million) in addition to a social NPV of nearly 530 million *nuevos soles* (US\$190 million). Additional details on the Project's economic and financial analysis are provided in Annex 6.

41. For the solid waste component, in order to determine the feasibility of applying the *fideicomiso* (fiscal intercept), it was necessary to review the revenue and capital expenditure of each Province and municipal District involved. This analysis indicates that most of the

municipalities can cover operating and maintenance costs estimated in pre-investment studies through intergovernmental transfers and tariffs. A few of the smallest municipalities may not be able to cover all operation and maintenance costs. The Bank is exploring options with the Regional Government in order to cover the deficit of resources for those special cases.

B. Technical

42. The preparation of the solid waste management and disaster risk management components were initiated under the PRRVV project. The investments have been analyzed in detail with feasibility studies during the preparation of the proposed Project. For the solid waste management system, the investments selected have undergone a study exploring alternatives to the various options for disposal, collection and recycling systems in the three provinces. Also, a series of South-South exchanges provided perspective on the available options, including a visit by local Peruvian officials to Colombia, which was of particular use in evaluating alternatives. The chosen alternative includes three landfills, one serving each of the provinces of Cusco, Calca and Urubamba, and investments in equipment for municipal District-level services of cleaning public spaces and streets, waste collection and recycling. The designs and specifications for these works are being finalized and will be the basis for contracting of works.

43. For the tourism component, the proposed subcomponents have been reviewed in detail by the Bank to ensure feasibility in terms of design and appropriateness to meet the Project objectives, ensure adequate institutional arrangements are in place for implementation, safeguards requirements are met, and that the Project is cost effective. In the case of disaster risk management, where a major objective is capacity building at lower levels of government, investments are of a significantly smaller size. The preliminary designs and costing are currently under preparation, to be finalized during implementation. The component will finance investments such as early warning systems, small mitigation works and the design of disaster risk management plans.

44. For the monitoring and evaluation of activities, the Project will support capacity building and development of a system, as COPESCO does not have a consolidated monitoring and evaluation system in place.

C. Financial Management

45. A Financial Management (FM) capacity assessment was performed to determine the adequacy of COPESCO's FM arrangements to support the proposed Project's implementation. Financial management tasks will be carried out by COPESCO's General Administrative Office (*Oficina General de Administración*, or OGA)¹⁵ in coordination with the PCU, both of which have experience implementing IBRD projects. The PCU's structure includes a Financial Management Specialist already familiar with Bank requirements; however, the OGA's structure will require strengthening in the accounting area. Though the Project Coordination Committee will provide inter-institutional coordination, lack of interaction and coordination with the provinces involved in project implementation may pose some challenges. Also, the operational and FM arrangements for the implementation of Subcomponent 1.2, the pilot Competitive Fund

¹⁵ The OGA is comprised of the Financial Unit, Procurement Unit and Human Resources Unit.

for Tourism (*fondo concursable*), will be prepared during project implementation as a disbursement condition for this Subcomponent. Moreover, availability of timely financial information may be affected if the interaction between the OGA and the PCU does not ensure timely recording of project transactions in the Integrated Financial Management System (*Sistema Integrado de Administración Financiera*, or SIAF). Audit contracting may be delayed due to cumbersome and complex procedures followed by the General Comptroller of Peru. On this basis, the FM risk is considered moderate. Proposed financial management arrangements are considered acceptable, subject to the: (i) submission of the updated version of the OM; and (ii) submission of the adjusted format of project financial reports. Additional actions required for implementation are established in Annex 3.

D. Procurement

46. An assessment of the implementation agency's capacity to implement procurement actions for the Project was performed in February and May, 2013. The capacity assessment reviewed the Procurement Unit in COPESCO in terms of: (a) the organizational structure; (b) facilities and support capacity; (c) qualifications and experience of the staff that will work on procurement; (d) record-keeping and filing systems; (e) procurement planning and monitoring/control systems used; and (f) capacity to meet Bank procurement contract reporting requirements. Based on the information available, the Bank has assessed the overall risk as high. The corrective measures that have been agreed to are: (i) adoption of the OM including, *inter alia*, procurement and contracting procedures, as a condition of effectiveness of the Loan Agreement; (ii) inclusion in the Loan Agreement of the Special Procurement Provisions; (iii) inclusion in the Loan Agreement of additional provisions related to Project implementation from a procurement point of view; and (iv) close monitoring by the Bank, particularly during the first two years of project implementation. Additional details are available in Annex 3.

E. Social (including Safeguards)

47. The proposed Project will deliver important benefits to the inhabitants of the Cusco region. The investments in solid waste management and disaster risk management will satisfy important needs of the Province of Cusco and the communities in the Sacred Valley. The restoration of historic and cultural heritage sites, the improved access to them and, in general, the enhancement of tourism infrastructure and services will also increase economic opportunities for local people.

48. One of the three landfills (Urubamba) will be built on municipal land. The other two (Cusco and Calca) require land acquisition. The land for the Cusco landfill will be acquired from an individual and the land for the Calca landfill will be acquired from an indigenous community. Abbreviated Resettlement Plans have been prepared for the Cusco and Calca landfills (Cusco disclosed in country on July 31, 2013, Calca on August 5, 2013 and disclosed on the Bank's external website on August 6, 2013, to be consulted when negotiation of the land acquisition takes place). The interventions planned in the Sacred Valley as part of the tourism services and disaster risk management components may require land acquisition. A Resettlement Policy Framework has been prepared to guide the preparation of resettlement plans during project implementation (consulted on August 2, 2013, disclosed in country on August 5, 2013 and disclosed on the Bank's external website on August 6, 2013).

49. The solid waste component will cause economic displacement among waste pickers. The component will construct new landfills that will replace existing dumpsites, which will affect the livelihoods of approximately 45 waste pickers. In addition, the changes in solid waste collection and disposal practices (including recycling) in the city of Cusco could affect the livelihoods of approximately 600 waste pickers. A Social Inclusion Plan has been prepared to address these impacts (disclosed in country on July 31, 2013, consulted on September 24, 2013 and disclosed on the Bank's external website on August 6, 2013).

50. A Social Assessment was carried out (consulted between April and June 2013, disclosed in country on August 5, 2013 and disclosed on the Bank's external website on August 6, 2013) to evaluate the potential effects of the project components on Indigenous Peoples. Two of the landfills (Calca and Urubamba) will affect communities of Indigenous Peoples. The Calca landfill will require the acquisition of community land and the Urubamba landfill will be built adjacent to community land. Indigenous Peoples Plans (IPPs) have been prepared for these subcomponents. The IPP for Urubamba was consulted in August 2013, disclosed in country on August 15, 2013 and disclosed on the Bank's external website on August, 15 2013. The IPP for Calca has been consulted and approved by the community of Vista Alegre Yanahuaylla (same dates as Urubamba) and is in the process of being approved by Parcco, a community adjacent to the landfill area. COPESCO and Parcco leaders have held three meetings (July 5, 31, and September 27 of 2013), during which the community indicated their satisfaction with the terms of the subcomponent and the strategy, but manifested interest in visiting other sites where similar projects have been implemented before giving its final approval. COPESCO and Parcco leaders are working towards meeting this demand and confirming their final, formal support for the IPP. The interventions planned in the Sacred Valley as part of the tourism and disaster risk management components may affect communities of Indigenous Peoples; an Indigenous Peoples Planning Framework has been prepared to address potential adverse impacts on these communities and to maximize project benefits for them (disclosed in country on July 27, consulted on August 2013 and disclosed on the Bank's external website on August 6, 2013).

51. The communities of Haquira and Ccorca are concerned about the record of poor management of the existing Cusco waste dump and the resulting contamination of the area around the dump and the access roads. The Province of Cusco is responsible for the closure of the waste dump and, under the Peruvian legal framework, must carry out a Rehabilitation Plan for the Degraded Area. The Project includes technical assistance to support the adequate closure of the dump. Additional details on social safeguards are available in Annex 3.

F. Environment (including Safeguards)

52. The Project is classified as Category A under OP/BP 4.01 based upon the one proposed moderately-sized landfill in Cusco (part of Component 2), even though this landfill is expected to improve the environmental sustainability of solid waste management in the region. The works associated with Components 1 and 3 involve relatively standard, smaller-scale infrastructure works with potential environmental and social impacts that have been assessed as short-term, not significant, and can readily be prevented or mitigated with standard measures. There are no significant negative indirect or long-term impacts anticipated related to the Project.

53. Related to Components 1 and 3, an Environmental and Social Management Framework (ESMF) has been developed (disclosed in country on August 1, consulted on August 2, 2013, 2013 and disclosed on the Bank's external website on August 6, 2013). Related to component 2, an Environmental and Social Impact Assessment (ESIA) has been developed for each of the three landfills, each including an Environmental and Social Management Plan (Calca and Urubamba consulted on July 11, 2013, Cusco on July 12, 2013, both disclosed in country on July 31, 2013 and disclosed on the Bank's external website on August 6, 2013). An analysis of alternatives related to the best technology to apply to waste disposal (e.g., several local landfills, a regional landfill, and other combinations, including transfer stations) was conducted for Component 2. A site selection analysis was also performed for each landfill including various technical, environmental and social factors (e.g., critical or sensitive natural habitats, forests, proximity to populated areas or to environmental designated protected areas), and included stakeholder input.

54. The Project does not anticipate any significant negative impact on physical cultural resources. The ESIA's for Component 2 landfills have not identified any potential likelihood of encountering physical cultural resources. However, several of the activities for Components 1 and 3 may take place directly within the limits or in the surrounding areas of archeological sites such as Ollantaytambo. Any environmental analyses, as part of the ESMF, associated with component 1 and 3 subcomponents will specifically include consideration of physical cultural resources. All subcomponent construction contracts will include procedures and requirements related to chance find management.

55. The PCU will be responsible for environmental management and has staff and experience related to Bank safeguards. Component 4 provides resources to support the PCU environmental safeguards management. The Component 2 landfill for Cusco will likely be contracted as a design-build-operate contract, which will require compliance with the specific landfill ESMP. It will have an independent supervision which will include the management of environmental and social aspects. The execution of works in components 1 and 3 will be contracted to construction companies, who will be required to comply with the environmental and social requirements developed under the ESMF and any applicable Peruvian regulatory requirements including related to culture heritage. Supervision of these works/activities will be contracted to consultants, who in addition to technical supervision will provide environmental and social supervision. The OM will include relevant environmental and social aspects, including compliance with project ESMF and ESIA's, inclusion of environmental and social conditions in project contracts, use of independent supervisors for project contracts, and supervision responsibilities of COPESCO. Safeguards instruments have been disclosed and consulted as per Bank policies. Details on environmental safeguards are provided in Annex 3.

Annex 1: Results Framework and Monitoring

Country: Peru

Project Name: Cusco Regional Development (P117318)

Results Framework

Project Development Objectives

PDO Statement

To improve the quality of tourism and solid waste management services and increase the resilience of the tourism sector to the impacts of natural disasters in the provinces of Calca, Urubamba, and Cusco.

These results are at Project Level

Project Development Objective Indicators

Indicator Name	Core	Unit of Measure	Baseline	Cumulative Target Values					Frequency	Data Source/ Methodology	Responsibility for Data Collection
				YR1	YR2	YR3	YR4	End Target			
Percent reduction in the dissatisfaction rating of the upgraded tourism sites under the Project	<input type="checkbox"/>	Percentage	0.00	0.00	0.00	0.00	0.00	30.00	Baseline to be carried out prior to the start of works and the second survey to be carried out within six months of completion	Visitor survey	COPESCO

									of works in each project site.		
Direct project beneficiaries	<input checked="" type="checkbox"/>	Number	0.00	0.00	0.00	516,310.00	1,135,929.00	1,146,719.00	Annual	INEI, COSITUC	COPESCO
Female beneficiaries	<input checked="" type="checkbox"/>	Percentage Sub-Type Supplemental	0.00	49.00	49.00	49.00	49.00	49.40	Annual	INEI, COSITUC	COPESCO
Number of people (tourists and residents) in the Project area from whom waste is collected and disposed in one of the Project sanitary landfills	<input type="checkbox"/>	Number	0.00	0.00	0.00	516,310.00	1,135,929.00	1,146,719.00	Annual	INEI, COSITUC	COPESCO, Provinces of Cusco, Calca and Urubamba
Number of people (tourists and residents) covered by a functioning early warning system for natural disasters under the Project	<input type="checkbox"/>	Number	0.00	0.00	0.00	689,584.00	703,044.00	703,044.00	Annual	INEI, COSITUC	COPESCO

Intermediate Results Indicators

				Cumulative Target Values					Data Source/	Responsibility for
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Indicator Name	Core	Unit of Measure	Baseline	YR1	YR2	YR3	YR4	End Target	Frequency	Methodology	Data Collection
Existing tourism sites equipped with improved infrastructure installments	<input type="checkbox"/>	Number	0.00	0.00	1.00	2.00	3.00	3.00	Annual	COPESCO	COPESCO
Pilot Competitive Fund for Tourism for small businesses in the Sacred Valley operational	<input type="checkbox"/>	Yes/No	No	No	No	No	Yes	Yes	Annual	COPESCO	COPESCO
Industrial and municipal waste disposal capacity created under the project	<input checked="" type="checkbox"/>	Metric ton	0.00	0.00	0.00	40.00	350.00	390.00	Annual	Provinces of Cusco, Calca and Urubamba	COPESCO, Provinces of Cusco, Calca and Urubamba
Informal and formalized recyclers (households) benefiting from Project social inclusion activities.	<input type="checkbox"/>	Number	0.00	0.00	0.00	40.00	102.00	102.00	Annual	Social Inclusion Plan	COPESCO
Number of Provincial sanitary	<input type="checkbox"/>	Number	0.00	0.00	0.00	2.00	3.00	3.00	Annual	COPESCO	COPESCO

landfills constructed under the Project											
Number of municipalities provided with equipment and works for improved collection, recycling and street sweeping	<input type="checkbox"/>	Number	0.00	0.00	8.00	12.00	16.00	16.00	Annual	Municipalities	COPESCO, Provinces of Cusco, Calca and Urubamba
Emergency Preparedness Plan established for tourists	<input type="checkbox"/>	Yes/No	No	No	No	No	Yes	Yes	Annual	COPESCO	COPESCO
Strategic Regional Plan updated for prevention and reduction of disaster risk	<input type="checkbox"/>	Yes/No	No	No	No	Yes	Yes	Yes	Annual	COPESCO	COPESCO

Methodology

Project Development Objective Indicators

Indicator Name	Description (indicator definition etc.)
Percent reduction in the dissatisfaction rating of the upgraded tourism sites under the Project	A baseline survey measuring levels of visitor satisfaction/dissatisfaction with specific aspects within the scope of the Project will be carried out immediately before beginning works. A completion survey will be carried out six months following the

	completion of the works. It will measure the percent reduction in share of visitors who indicate that they are not fully satisfied with their visit to the site, as typically tourist satisfaction rates are high overall for Cusco and the Sacred Valley and the incremental increase in overall satisfaction would be low and difficult to measure.
Direct project beneficiaries	Direct beneficiaries are people or groups who directly derive benefits from an intervention (i.e., children who benefit from an immunization program; families that have a new piped water connection). Please note that this indicator requires supplemental information. Supplemental Value: Female beneficiaries (percentage). Based on the assessment and definition of direct project beneficiaries, specify what proportion of the direct project beneficiaries are female. This indicator is calculated as a percentage.
Female beneficiaries	Based on the assessment and definition of direct project beneficiaries, specify what percentage of the beneficiaries are female.
Number of people (tourists and residents) in the Project area from whom waste is collected and disposed in one of the Project sanitary landfills	This includes the number of residents and tourists in the Project area of the Provinces of Cusco, Calca and Urubamba whose waste is collected and disposed in one of the Project sanitary landfills. Demographic and tourist data was used from INEI and COSITUC, respectively, along with the projection that the Calca and Urubamba sanitary landfills will be complete in year 3 and the Cusco landfill in year 4 to estimate the total number of beneficiaries. Data reflecting the total number of annual tourists visiting the Sacred Valley was available, but the breakdown between Cusco, Calca and Urubamba had to be inferred from 2011 COSITUC data. The proportion of annual tourists visiting Ollantaytambo was used to represent the proportion of the annual tourists in the Sacred Valley in the Province of Urubamba (67%). The remaining 33% were assumed to have visited Pisac, in the Province of Calca. The Province of Cusco was assumed to receive 100% of the annual tourists visiting the Sacred Valley. The same data was used to estimate Direct project beneficiaries.
Number of people (tourists and residents) covered by a functioning early warning system for natural disasters under the Project	Data from INE, COSITUC and INDECI reflect the number of tourists and total population living in the municipalities in which the early warning systems will be installed. It is projected that the Ollantaytambo system will be installed in year 3 and the Calca Cochoc, Pisaq and Vilcanota systems will be installed in year 4.

Intermediate Results Indicators

Indicator Name	Description (indicator definition etc.)
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Existing tourism sites equipped with improved infrastructure installments	COPESCO will monitor progress on sites equipped with improved infrastructure installments and will provide annual reports.
Pilot Competitive Fund for Tourism for small businesses in the Sacred Valley operational	Expected to be operational by Projects closure. COPESCO will provide annual reports on its progress.
Industrial and municipal waste disposal capacity created under the project	This indicator measures the municipal or industrial solid waste disposal capacity created as a result of the project. The baseline for this indicator is zero.
Informal and formalized recyclers (households) benefiting from Project social inclusion activities.	A baseline of the informal recyclers within the Project area has been established by the Project's Social Inclusion Plan. COPESCO will monitor participation in the Project's social inclusion activities and will provide annual reports.
Number of Provincial sanitary landfills constructed under the Project	Reports on the progress of landfill construction to be provided annually by the provinces of Cusco, Calca and Urubamba.
Number of municipalities provided with equipment and works for improved collection, recycling and street sweeping	Data to be collected annually by the provinces of Cusco, Calca and Urubamba.
Emergency Preparedness Plan established for tourists	Expected to be completed by Project closure. COPESCO will provide annual reports on its progress.
Strategic Regional Plan updated for prevention and reduction of disaster risk	Expected to be completed by Project closure. COPESCO will provide annual reports on its progress.

Annex 2: Detailed Project Description

PERU: Cusco Regional Development Project

1. Machu Picchu, via the city of Cusco, is the main tourism destination in Peru, attracting close to 90% of foreign visitors as well as many domestic visitors. As tourism has grown from year to year, the number of visitors to Cusco and to attractions in the Sacred Valley has also grown from year to year; however, the underlying infrastructure supporting this growth has not kept pace.

2. The proposed Project will support strengthening of the tourism sector in Cusco and the Sacred Valley through interrelated components for the consolidation of existing tourism sites, solid waste management and disaster risk management, which are complemented by a fourth component for institutional strengthening.

3. *Component 1: Development and Consolidation of Tourism Services (US\$25million, of which US\$18.8 million is Bank-financed).* The objective of this component is to improve the quality and coverage of tourism services in the Sacred Valley and surrounding areas. The component will achieve this through, *inter alia*, (i) consolidating “classic” tourist attractions by improving and expanding infrastructure, providing improved access to sites, internal walkways and signage, and (ii) developing small and microenterprises through a pilot Competitive Fund for Tourism (*Fondo Concursable*), providing technical assistance and knowledge to position small and microenterprises in the market.

4. *Subcomponent 1.1: Consolidation of Tourism Services:* A series of subcomponents are included in this subcomponent, consisting of small infrastructure projects to improve visitor experience in Písaq, Ollataytambo, and tourism circuits in the Sacred Valley across the provinces of Calca, Cusco and Urubamba. Examples of investments include the following:

(a) The subcomponent in Písaq includes investments to upgrade facilities, including restrooms, administrative offices, a small medical station, a ticket office and to provide more space for parking. The subcomponent also includes the creation of a space for local artisans to sell crafts. Also included are improvements to foot paths in the archaeological park. Within the site, the component will support the building of an underground center from which visitors will be distributed to different routes. Additionally, the component will support improving the trails within the site, installing handrails as well as informative and interpretive signage. The trail improvements include the construction of a pedestrian bridge over the river, improved lighting, reinforcement of concrete arches, implementation of steel cables, upgrading of the road surface and the installation of a local interpretive center. Finally, this subcomponent includes the improvement of an access road of about nine kilometers in length with asphalt replacement, drainage, widening to allow for tour buses to pass more easily in both directions, and vulnerability reduction through slope stabilization.

(b) In Ollantaytambo, the proposed subcomponent includes the installation of signage for key cultural assets within the fortress. It also aims to improve pedestrian access through staircases and railings to an adjacent site, as the existing staircase is unstable and precarious. The proposed subcomponent also includes enhanced access to Pumamarca, a less-visited archaeological site due to poor access and maintenance. This enhancement includes the construction of a tourist center with restrooms, a ticket office, a small parking lot, trail connections, a craft square, and hiking paths. It would also support improved access through improvements and drainage on the existing path.

5. Other proposed subcomponents include the implementation of observation points for viewing the attractions along the touristic routes within the Sacred Valley. The Project proposes to upgrade the existing observation points, which are currently are being used in an insecure and transient manner. The Project supports improvements including parking areas, rest areas, establishment of a location for craft sales, and informative and interpretive signage.

6. *Subcomponent 1.2: Competitive Fund for Tourism (Fondo Concursable).* This subcomponent is comprised of a pilot *Fondo Concursable*, aimed at improving the competitiveness of small-scale tourism products and services such as artisanal and cultural products. The principal objective of this subcomponent is to strengthen tourism services within the Sacred Valley with a network providing local inputs and the commercialization of such services as lodging, restaurants, travel services as well as promoting Andean culture through the arts.

7. This fund is still in the initial design stage and will be developed during implementation. COPESCO has carried out a market study to assess the current demand for this type of instrument to determine the amount of funds the area of intervention can reasonably absorb. It has been agreed that this fund will not transfer funds directly to small and microenterprises, but will provide technical assistance to these businesses to support their access to the tourism market in the Sacred Valley.

8. *Subcomponent 1.3: Technical Assistance for the Strengthening of Tourism Services.* This subcomponent provides technical assistance through a series of studies that will evaluate the (i) maximum capacity at the classic tourism attractions; (ii) appropriate fee rate for the various sites in the Sacred Valley; (iii) operation and maintenance costs of the assets linked to tourism services; and (iv) fee collection and distribution mechanisms and patterns in the use of tourism fees. It is expected that these studies will provide a basis for recommendations for the optimized level and use of tourism fees that may be used to propose modifications in Law No. 28719, which governs the collection and use of these fees.

9. This subcomponent also includes activities directed towards strengthening public-private coordination and cooperation, supporting activities to increase the participation of public-private partnerships in the management of tourism products and services. The subcomponent supports the commercialization and diffusion of the improved offerings of the Sacred Valley tourism circuit. The activities' principal objective is to make the Sacred Valley a tourist destination in

high demand nationally and internationally. These activities will benefit from the greater participation of public-private partnerships to strengthen the commercialization framework. Print and virtual promotional literature will be produced on a large scale, and technical assistance will be provided to public and private initiatives for product design, press tours, and management of information technologies and social networks.

10. *Component 2: Integrated Solid Waste Management (US\$18.4 million, of which US\$13.8 million is Bank-financed).* The objective of this component is to improve local capacity to clean streets and public spaces and to efficiently collect, transport and dispose of solid waste in the provinces of Cusco, Calca and Urubamba. The component will achieve this through, *inter alia*, (i) investments in Provincial solid waste services to improve solid waste disposal and composting; (ii) investments in municipal District-level solid waste services to improve collection, recycling, and cleaning of streets and public spaces; (iii) technical assistance and capacity building for improved solid waste services; and (iv) communication on the implementation of project works and the promotion of adequate waste management practices in communities. The solid waste management component was designed in a holistic manner as a system for waste collection, transportation, disposal and treatment considering the Province and municipal District-level needs and in accordance with the national regulations in force.

11. *Subcomponent 2.1: Improved Infrastructure and Equipment and Supporting Activities:* This subcomponent will finance improved infrastructure and equipment for solid waste services for the Provincial and municipal Districts of the Provinces of Cusco, Calca and Urubamba. It will also provide technical assistance and capacity building for improved solid waste services, as well as support for communication and educational programs.

12. *Investments in Provincial solid waste services:* The Project will support the development of modern disposal facilities by financing the construction of a landfill and a pilot composting facility in each of the three provinces. It will finance the construction (and supervision of works) of three landfills in total, designed to receive the waste from the provinces of Cusco, Calca and Urubamba and of the three small composting facilities located on the landfill sites and implemented on a pilot basis. The Cusco Provincial landfill will have an estimated capacity of 350 tons per day. The landfill in Calca will have a capacity of 15 tons per day and the one in Urubamba of 25 tons per day.

13. *Investments in municipal District-level solid waste services:* The Project will support investments in equipment to improve the solid waste services provided by municipal Districts. These include the cleaning of streets and public spaces, as well as waste collection. Such investments would for instance include the procurement of compactor trucks, according to the amount of solid waste to be collected and transported for disposal, and the distance and type of geography of the area. They would also include equipment for municipal District-level recycling programs that support the social inclusion of the informal waste sector.

14. *Technical assistance and capacity building for improved solid waste services:* This subcomponent is intended to improve the capacity of the Provincial and municipal Districts to provide solid waste management services, specifically through the provision of Professionalization services. Professionalization contracts are designed to improve management,

human resources, administration, fee collection and technical operation and supervision. Human resource certification programs in the solid waste management sector will be designed and implemented to strengthen the knowledge and management skills in the sector and formalize human resources standards. This capacity building will be provided to all provincial and district municipalities under the project through a multi-year contract with a consulting firm.

15. Communication programs for works under Component 2 and for the promotion of adequate waste management practices to the communities: The project will finance the continuous consultation process that will accompany the implementation of works. This includes the provision and dissemination of information on the project progress, the environmental management plan and Social Inclusion Plan implementation. It will also finance the development and implementation of educational and public communication campaigns on topics such as litter prevention, source separation, and tariff implementation.

16. *Subcomponent 2.2. Technical Studies including Social Inclusion Plan for Informal Recyclers.* This subcomponent will provide the technical assistance needed for implementation of the Social Inclusion Plan for informal recyclers, which includes formalization of the informal waste sector as part of the municipal recycling systems, social support programs, and alternative livelihood programs. It will also finance technical studies to support the project investments and future related investments, such as a specific study on the closure of existing dumpsites.

17. *Component 3: Disaster Risk Management and Disaster Preparedness (US\$2.6 million, of which US\$1.9 million is Bank-financed).* The objective of this component is to increase the resilience of the local population, tourists, and infrastructure in touristic areas with high vulnerability to natural disasters.

18. *Subcomponent 3.1: Implementation of Disaster Risk Management Systems.* This subcomponent will achieve this through, *inter alia*, (i) designing and implementing early warning systems for the flooding of the Vilcanota and Patacancha Rivers in the Sacred Valley and Ollantaytambo; (ii) designing and implementing an integrated approach to the reduction of geological and climatic risks in the micro basin of K'itamayu in Pisac; and (iii) designing and implementing an integrated approach to mitigate external geodynamic risks in the Ccochoq river basin in Calca.

19. These activities will reduce the disaster risk through the implementation of structural and non-structural measures in the Sacred Valley. The structural subcomponents would include river and micro basin protection; landslide protection measures, and other small civil works to protect the tourist infrastructure and basic infrastructure providing access to tourism circuits, including access roads and bridges. The non-structural activities would include the design and installation of three early warning systems based on modeling of future scenarios including climate change.

20. *Subcomponent 3.2: Planning and Capacity Building for Disaster Risk Management.* This subcomponent supports the development of an updated Disaster Risk Management Plan for the Sacred Valley as well as plans for the evacuation of tourists enhanced communication systems at community level, preparation of the participative plans for evacuation, training and simulation of exercises with the local population and tourists. Additionally, the Project will strengthen the

local capacity in the municipalities according to the legal and institutional framework for disaster risk management.

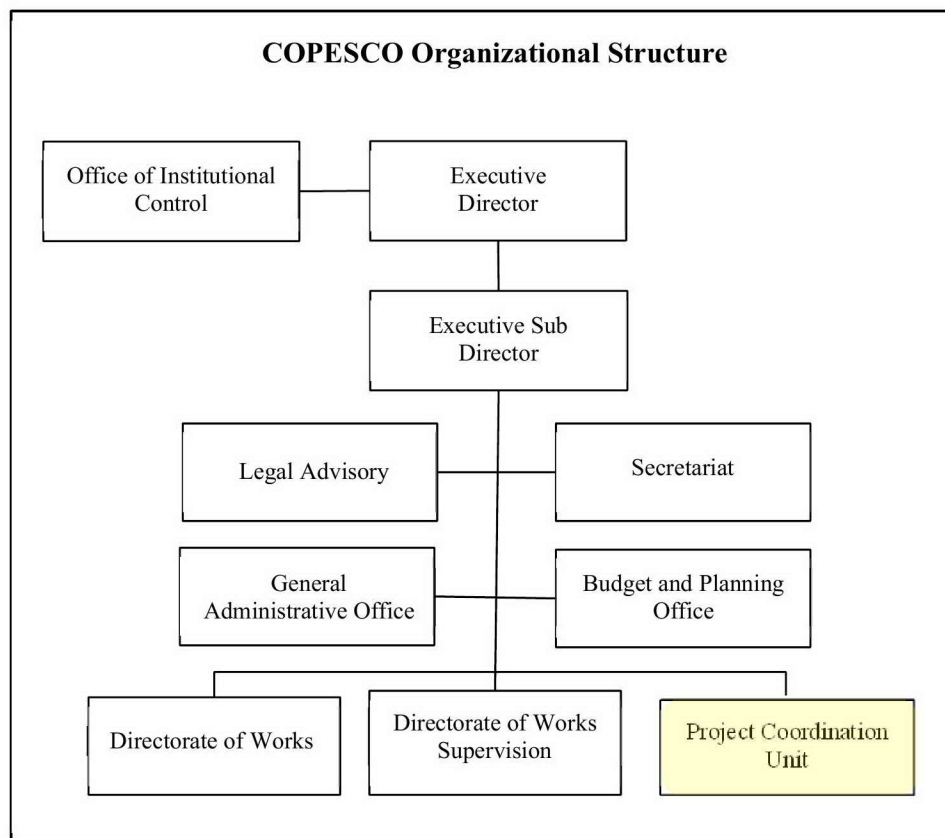
21. *Component 4: Institutional Strengthening, Management and Monitoring and Evaluation (US\$6.1million, of which US\$0.5 million is Bank-financed).* This component will support the capacity building of the principal institutions involved in the operation of tourism activities in the Sacred Valley, and COPESCO, including its PCU. Activities will include, *inter alia*, (i) collection of baseline data for later evaluations and follow up analyses; and (ii) enhanced capacity for project management, project audits, and monitoring and evaluation of project results. This component includes support for the strengthening of the PCU in terms of hiring additional technical specialists, and fiduciary and safeguards staff.

Annex 3: Implementation Arrangements

PERU: Cusco Regional Development Project

1. The CRG will have overall responsibility for the Project, with COPESCO serving as the implementing agency. An institutional assessment of COPESCO has been carried out and used to determine staffing and organizational arrangements for the Project. Figure A3.1 illustrates the organizational structure of COPESCO. The Project design includes capacity building and implementation support, providing the implementing agency with the necessary tools and training to carry out their functions more effectively. The implementation of the Project is expected to be five years.

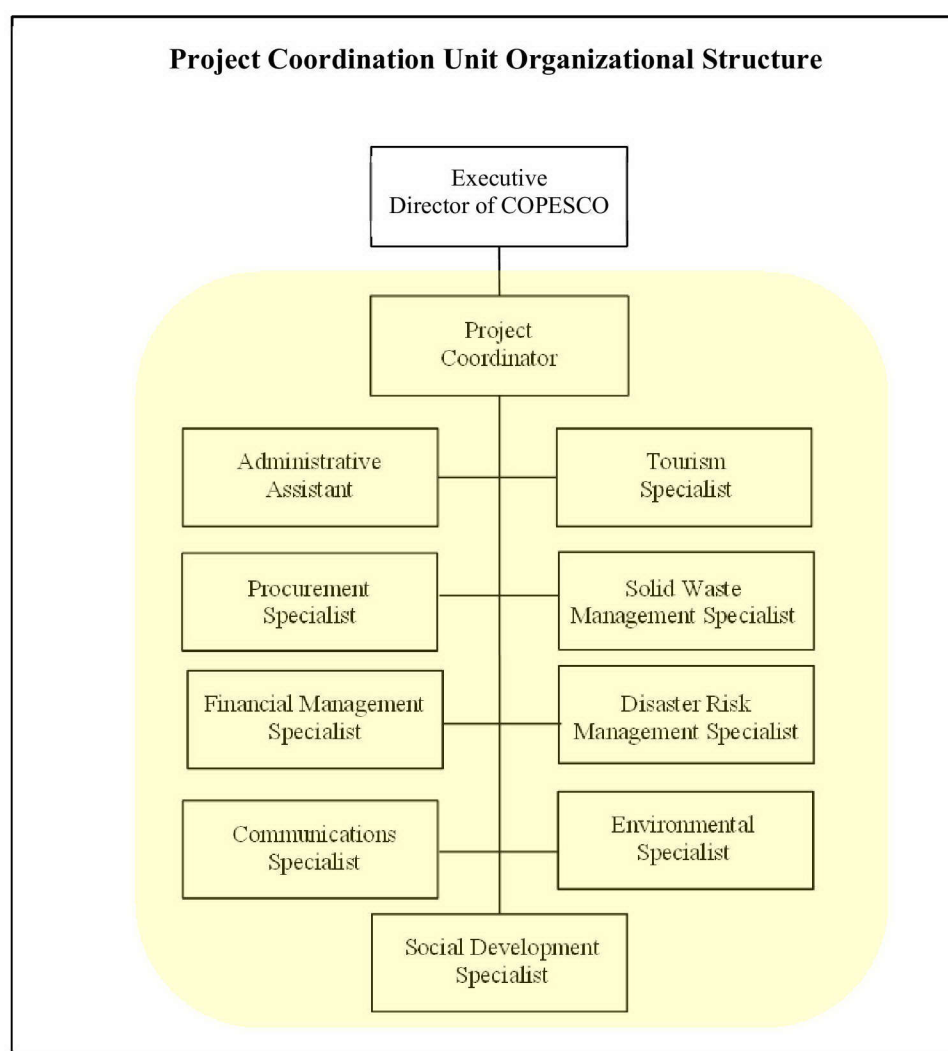
Figure A3.1: Organizational Structure of COPESCO



2. *Implementing Agency.* COPESCO is the implementing agency and has established a PCU that will be responsible for overall implementation and will coordinate the actors involved in the Project's execution. This unit within COPESCO builds on the previous capacity built through the PRRVV to ensure an adequate implementation pace and to allow for accountability. Figure A3.2 below illustrates the organizational structure of the PCU within COPESCO. The fiduciary team of the PCU in particular has experience executing World Bank-financed projects, including the procurement of small civil works and contracting of consultants. The PCU will be responsible for implementation of all Project activities, internal and external communications, financial management, procurement and compliance with safeguards. The PCU will also coordinate with relevant subnational and national institutions on component implementation. The main

responsibilities of the PCU in implementing Project components include: (i) preparing technical reports and managing the No Objection process with the Bank for all procurement processes; (ii) prepare TORs; (iii) evaluate and prepare reports on the completion and quality of studies, plans, activities, technical specifications for works, and Project indicators; and (iv) supervise the progress of consultancies and works, among others further detailed in the OM. The PCU will be staffed with personnel from COPESCO and will be strengthened as needed with additional staff and consultants to ensure adequate capacity. The minimum staffing requirement for the PCU as defined in the OM includes the Project Coordinator, Tourism Specialist, Solid Waste Management Specialist, Disaster Risk Management Specialist, Social Specialist, Environmental Specialist, Procurement Specialist, Financial Management Specialist, Communications Specialist, and Administrative Assistant.

Figure A3.2: Organizational Structure of the PCU

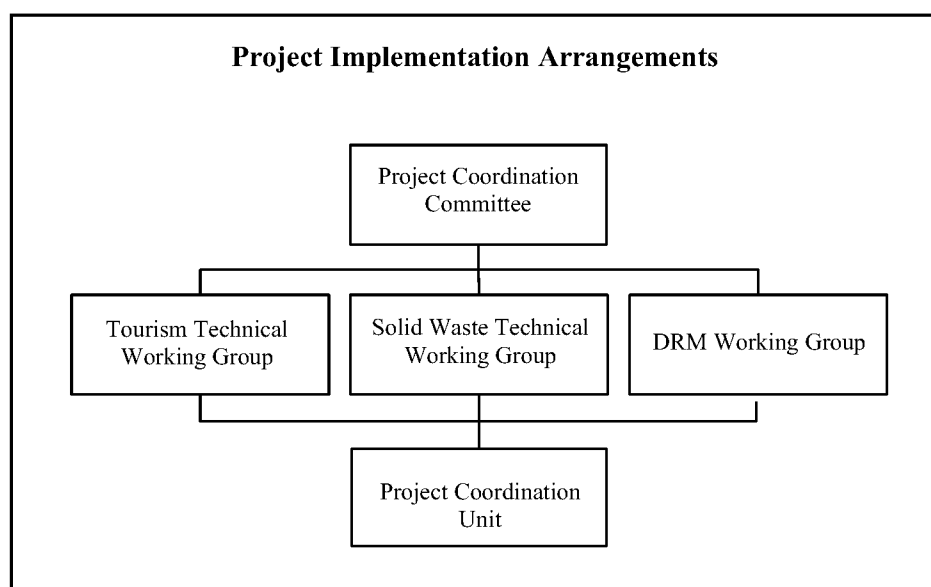


3. *Project Coordination Committee.* This committee will be established by the GRC in order to provide high level coordination of the Project and ensure Project alignment with broad strategic objectives. The main responsibilities of the Project Coordination Committee in

implementing Project components include: (i) facilitating the inter-institutional coordination between the national level sectoral entities, the regional government, local governments involved and civil society organizations; (ii) recommending actionable policies within the framework of development strategies; (iii) providing support in aligning strategies of common interest among entities; and (iv) proposing communication strategies and implementing resolution mechanisms for operational issues. The Committee will include representatives from the key government institutions and civil society stakeholders, for example, representatives from MEF, the CRG, the three participating Provinces (Cusco, Calca and Urubamba) and other stakeholders. The TORs for the Committee, including the membership and meeting frequency, are included in the OM, to be adopted prior to effectiveness.

4. *Technical Working Groups.* The Project Coordination Committee will establish technical working groups for each component. These working groups (one for tourism, one for solid waste and one for disaster risk) will operationalize the decisions reached at the Coordination Committee level and will bring together relevant technical specialists from different subnational institutions (Municipal Districts, Provinces, the CRG, and professional associations) in order to provide technical reviews of current and future activities. These working groups will ensure that the municipalities and technical staff are fully engaged in the implementation process, as these stakeholders will eventually be responsible for operations and maintenance of assets financed under the Project. The main responsibilities of the Technical Working Groups in implementing the Project components include: (i) providing professional and technical opinions on relevant aspects of program, project and activity implementation led by the PCU; and (ii) developing proposals, exchanging opinions to be submitted to the PCU. The TORs for the technical working groups, including composition and meeting frequency, are included in the OM. Figure A3.3 illustrates the project implementation arrangements between the Project Coordination Committee, the Technical Working Groups and the PCU.

Figure A3.3: Project Implementation Arrangements



5. *Implementation Arrangements for the Tourism and Disaster Risk Management Components:* The PCU will be responsible for implementing the Tourism and Disaster Risk Management Components, including procurement and contract management. The construction of works has been agreed as part of the technical design for each investment and will be coordinated also with the Technical Working Groups. The staffing plan for COPESCO has taken into account the need to strengthen the PCU's technical capacity for preparing and implementing investments for these components.
6. *Implementation Arrangements for the Solid Waste Component:* The basic implementation arrangements for the construction and operation of these facilities have been agreed upon and the detailed description and draft agreements are in the process of being elaborated.
7. The responsibility for bidding and construction supervision will lie with COPESCO in coordination with the solid waste technical working group. COPESCO will be provided with consultants to strengthen their technical capacity to evaluate bids for landfill investments and supervise the construction.
8. Upon completion of the works, COPESCO will transfer the works and goods to the municipalities responsible for the operation. Under Peruvian law, each of the Provinces will be responsible for final disposal services, while the municipal Districts will be responsible for collection, recycling, and cleaning of streets and public spaces.
9. Each of the municipal Districts will operate their collection, recycling and cleaning programs themselves through their municipal divisions in charge of these services and will be responsible for funding the operation and maintenance of these services. As part of their collection service they will be responsible for collecting and transporting the waste to the Provincial landfill for disposal and for paying fees to the Provincial government for this disposal.
10. Each of the Provinces will be responsible for the operation of their respective landfill and for disposing the wastes from the municipal Districts under their jurisdiction. The preference of the provinces is to contract out the operation of the landfills to a private operator that is the same contractor that would construct the landfill. This would follow a design-build-operate (DBO) contractual scheme with the private company having two clients in contractual terms, one with COPESCO (for the design-build) and the second with the province (for the operation, for a period of three years). The viability of the application of this type of contract in the context of the Project and the market for private companies interested in this type of contract is being evaluated and may not be applied to all three provinces. In particular the contractual arrangements under Peruvian law are being evaluated and, although the market for a private operator in Cusco is likely to be good, due to the small size of the landfills in Calca and Urubamba, private operators may not be interested. This will be evaluated and if it is not viable in these provinces, the alternative of providing a turn-key contract with a few months of operation and capacity building of the provinces for direct operation of the landfill will be considered. According to the Project Procurement Plan, the estimated date for procuring solid waste management equipment is April 21, 2014 and the estimated date for opening bidding for the works is May 5, 2014. Regardless of the approach taken, COPESCO is committed to meeting these dates to avoid delays in implementation.

11. An agreement will be made between each of the three Provinces and each of the municipal Districts under their respective jurisdictions. This agreement will outline the responsibilities of the municipal District and the Provinces; the tariffs charged for final disposal, and associated provisions such as fines for non-compliance and payment.

12. The coverage of the operational costs of the landfill and the collection systems, regardless of the level of cost recovery achieved, will be guaranteed using the *fideicomiso* mechanism, or fiscal intercept of financial resources transferred from the central government to the regional government and municipalities arising from income generated by oil revenues. This intercept is expected to provide financing that would be used to cover the costs of solid waste services not covered by cost recovery mechanisms and thus act as a guarantee for the operations and maintenance costs.

Financial Management and Disbursement Arrangements

13. As part of the preparation process of the proposed Project, a FM capacity assessment was performed to determine the adequacy of COPESCO's FM arrangements to support project implementation. In accordance with proposed institutional arrangements, the Project will be implemented by the CRG through its implementing agency, COPESCO, with the support of the existing PCU within COPESCO. Within those arrangements, FM tasks will be carried out by COPESCO's OGA in coordination with the PCU, both of which have gained experience implementing the PRRVV and trust fund activities and have maintained acceptable FM arrangements, which are now being strengthened to better respond to project needs. The PCU's structure includes a Financial Management Specialist, already familiar with Bank requirements; however, the structure of COPESCO's OGA will require strengthening in the accounting area. Though the Coordination Committee will provide inter-institutional coordination, lack of interaction and coordination with provinces involved in project implementation may pose some challenges. Also, the operational and financial management arrangements for the implementation of Subcomponent 1.2, the pilot Competitive Fund for Tourism (*Fondo Concursable*) have not yet been developed but will be finalized during project implementation as a disbursement condition for this Subcomponent. Moreover, availability of timely financial information may be affected if the interaction between COPESCO's OGA and the PCU does not ensure timely recording of project transactions in the Integrated Financial Management System (*Sistema Integrado de Administración Financiera*, or SIAF). Audit contracting may be delayed due to cumbersome and complex procedures followed by the General Comptroller of Peru. On this basis, the FM risk is considered moderate.

14. Based on progress reached, proposed financial management arrangements are considered acceptable, subject to the submission of the OM reflecting FM arrangements, to be adopted prior to effectiveness. Additionally, selection and contracting of an experienced accountant and accountant assistant under COPESCO's OGA will be carried out under TORs approved by the Bank within two months after effectiveness. Definition of acceptable operational arrangements, including FM, for the implementation of Subcomponent 1.2, *Fondo Concursable*, will be coordinated with the Project and approved by the Bank before disbursements start under Category 2 of the table of loan proceeds.

SUMMARY OF FINANCIAL MANAGEMENT ARRANGEMENTS

15. **Organizational Arrangements and Staffing.** FM tasks will be carried out by COPESCO's OGA in coordination with the PCU. The PCU's FM Specialist will be responsible for the preparation of the annual project budget, recording of information in the SIAF-MEP module, project financial reporting, and general coordination with the OGA. The OGA will be strengthened by an experienced accountant (responsible for budgeting, accounting and overall execution of the project budget through the SIAF), and an accountant assistant (to support tasks under the Project in coordination with the PCU FM Specialist), both financed out of loan proceeds, under TORs approved by the Bank. Detailed roles and responsibilities are reflected in the OM.

16. **Programming and budgeting.** Regional Governments with executing units are subject to local government rules. The PCU will prepare the project annual programming, procurement plan and budget (approved by Project Coordinator) to be reviewed and approved by COPESCO's Planning Office and incorporated into its annual budget. COPESCO's annual budget (including the proposed Project) will be approved by the Executive Directorate and later submitted to the CRG's Council for final approval. The project budget will be executed through the SIAF. The Budgeting and Planning office of COPESCO records the approved budget by financing source and monitors it. The Project OM will describe detailed processes and procedures, including required coordination between the PCU, COPESCO's Planning Office, and the CRG to enforce timely preparation and approval of the budget, and adequate recording and control of budget execution.

17. **Accounting and Information System.** COPESCO must comply with Peru's local requirements governing FM (including accounting policies and procedures and the use of the SIAF). Project transactions will be recorded in the SIAF and uploaded into the SIAF-MEP, which allows information to be organized by project components and subcomponents for project financial monitoring and preparation of Statement of expenditures (SOEs). Recording and processing of project transactions in the SIAF (commitment, accrual and payment) will be the responsibility of the OGA, while recording into the SIAF-MEP will be the responsibility of the PCU's FM Specialist.

18. **Recording in the SIAF-MEP.** Per the procedure established for the operation of this module, once the date of payment (date on which the check is delivered) is entered in the SIAF, payments (with loan proceeds and local counterpart) are captured by this module, the exchange rate is entered and expenditures are classified by project component and cost category in US dollars, which allows for the preparation of financial reports. Availability of timely financial information will require ensuring that payment receipts are immediately submitted by COPESCO's OGA to the PCU to complete the recording of project expenditures in the SIAF-MEP.

19. **Internal control.** Overall processes and procedures followed under the Vilcanota project and SFLAC Trust Fund required close coordination between the PCU and the OGA, which proved to be adequate. The Project will follow the same processes and procedures, strengthening them as required for further efficiency specifically for a timely recording of transactions and

management of a pilot Competitive Funds for Tourism under subcomponent 1.2, for which operational arrangements will be defined during implementation. Detailed processes and procedures designed for the Project are reflected in the OM under the FM section.

20. Within COPESCO is the Internal Audit Office, which reports to the General Controller's Office of Peru and includes reviews of the projects implemented by COPESCO. If such audits occur, the implementing agency will provide the Bank with copies of internal audit reports covering project activities and financial transactions.

21. **Financial Reporting.** The PCU in coordination with COPESCO's OGA will prepare the project financial reports on a cash accounting basis, based on the information provided by the SIAF-MEP in US dollars and classified by project components.

22. **Interim financial reports (IFRs)** will include: (i) a statement of sources and uses of funds and cash balances; (ii) a statement of investments, including information on the execution of the semester and accumulated; and (iii) respective explanatory notes to the financial statements; to be submitted not later than 45 days after the end of each calendar semester. On an annual basis, COPESCO will prepare the same financial reports mentioned above to be audited and submitted to the Bank. The core format and content of the IFRs have been agreed and the final version of these reports is satisfactory to the Bank. Moreover, the SIAF-MEP for loans is required to be installed for the Project before implementation begins.

23. **Auditing arrangements.** Annual project financial statements will be audited, following International Standards on Auditing, by an independent private firm and in accordance with the TORs acceptable to the Bank and following the framework of the established Memorandum of Understanding.¹⁶ The contracting period will be requested for at least the first three years of project implementation. The audit report will include: (i) an opinion on project financial statements; and (ii) a section on the adequacy of the internal control of the implementing agency in relation to the Project. The report will be submitted to the Bank no later than six months after the end of each fiscal year and will be financed out of loan proceeds. In accordance with the World Bank access to information policy, audited financial statements of the Project will be made publicly available.

24. **Flow of Funds and Disbursement Arrangements.** The Project will use the disbursement methods of reimbursement, advance and direct payment. Under the advance method, COEPSCO's OGA will open a designated account in US dollars to be maintained in the *Banco de la Nacion* and advances will follow Bank's disbursement policies and procedures. SOEs will be directly issued from the SIAF-MEP module, which provides with adequate controls. For payment processing, COPESCO's OGA in coordination with its PCU will withdraw the required amount to a local currency operating bank account from which payments to consultants, contractors and suppliers will be made based on a financial programming.

25. For counterpart funds, COPESCO has a single bank account in which receives all funds allocated by the CRG according to the budget approved, from which payments will be processed

¹⁶Memorandum of Understanding to be signed between the Bank and the General Comptroller Office of Peru.

under the Project through checks or deposits into the bank accounts of suppliers and will be recorded in the SIAF-MEP.

26. The ceiling for advances to be made into the designated account will be US\$1,000,000 and the frequency for reporting eligible expenditures will be at least quarterly. The minimum value of applications for direct payments or reimbursements will be reflected in the Project's Disbursement Letter.

27. As explained above, disbursements under Category 2 linked to the pilot *Fondo Concurable* under Subcomponent 1.2 will be subject to a disbursement condition.

28. Retroactive Financing will be available for payments made up to twelve months prior to the date of the Loan Agreement, following Bank procurement procedures, and such payments may not exceed 20 percent of the loan amount.

Table of Loan Proceeds

Category	Amount of the Loan (in USD)	Percentage of expenditures financed (exclusive of Taxes)
(1) Goods, works, non-consulting services, consultant services, training and Workshops under Component 1, except activities under subcomponent 1.2 of the Project.	15,916,647	100%
(2) Goods, non-consulting services, consultants services, training and workshops under pilot of Subcomponent 1.2 of the Project	2,868,750	100% (disbursement condition)
(3) Goods, works, non-consulting services, consultants services, training and workshops under Component 2 of the Project	13,821,707	100%
(4) Goods, works, non-consulting services, consultants services, training and workshops under Component 3 of the Project	1,917,464	100%
(5) Goods, non-consulting services, consultants services, training and workshops, Operating Costs and financial audits under Component 4 of the Project.	475,432	100%
TOTAL AMOUNT	35,000,000	

Procurement

29. *Country.* The national procurement system of Peru has made significant progress in the last few years, particularly with regards to access to information and adoption of standard bidding documents. However, it still suffers from serious setbacks that affect both the efficiency and transparency of government purchasing. Of most concern is the distortion of competition generated by the use of the referential price and the permanent concern for compliance with the

requirements set forth in the national regulatory framework, as well as the lack of procurement capacity in some sectors, particularly at the local level.

30. *Agency.* Following the implementation arrangements, COPESCO, within the CRG, will be responsible for the administration of the Project, including procurement, disbursement and FM matters of this operation. The Procurement team will be composed of two Procurement Specialists, who will be assisted by two Procurement Assistants, one for Component 1 and the other for Components 2 and 3. All procurement staff will be in place within 120 days after effectiveness. The CRG will keep the PRRVV fiduciary specialists in the PCU in order to ensure adequate capacity to conduct procurement under this proposed operation. COPESCO will strengthen its procurement unit through the hiring and training of staff in civil works contract administration, develop the DBO bid document for the Component 2, and supervision services.

31. *Operations Manual.* As part of Project preparation, CRG will prepare the OM, which provides detailed procurement information for the project's implementation, to be adopted by effectiveness.

32. *Bidding documents.* The CRG will prepare Bidding Documents for Project implementation in the first six months after the effectiveness with special attention to the DBO contracts.

33. *Procurement Special Provisions.* In addition and without limitation or restriction to any other provisions set forth in this section or in the Procurement Guidelines, the following provisions shall govern the procurement of goods and works with National Competitive Bidding procedures:

- (a) Foreign Bidders shall not be required to be locally registered as a condition of participation in the selection process.
- (b) No reference value ("*precio referencial*") shall be required for publication in the bidding documents or used for the purpose of evaluation.
- (c) Award of contracts shall be based exclusively on price and, whenever appropriate, shall take into account factors that can be quantified objectively, and the procedure for such quantification shall be disclosed in the invitation to bid.
- (d) Foreign Bidders shall be allowed to participate without restrictions and shall not be subject to any unjustified requirement which will affect their ability to bid such as, but not limited to, the requirement to authenticate their bidding documents or any documentation related to such bidding documents with either Peruvian Consulates, the Ministry of Foreign Affairs, or any Peruvian authorities as a prerequisite of bidding.
- (e) The Borrower, through the PCU, shall use standard bidding documents and standard evaluation formats, all satisfactory to the Bank.

34. In addition, and without limitation or restriction to any provision set forth in this section or in the Consultant Guidelines, the following provisions shall govern all employment of consultants:

- (a) Foreign Consultants shall not be required to be locally registered as a condition of participation in the selection process.

(b) Foreign Consultants shall not be required to authenticate any documentation related to their participation in the selection process with the Peruvian Consulates, the Ministry of Foreign Affairs, or any other Peruvian authorities as a condition of participation in said selection process.

(c) The Borrower shall use standard requests for proposals and standard evaluation formats, all satisfactory to the Bank.

(d) Foreign Consultants, either individuals or firms, shall not be required to pay fees to the Peruvian Consultants' Association that are different from those required for Peruvian consultants.

(e) No consultant hired for the Project, at the time he or she is carrying out his or her contractual obligations as a consultant, may hold civil service office or any other position in any agency of the Borrower, nor shall such consultant have any right to re-entry into any such office or position upon the conclusion of his or her consulting services.

A. General

35. Procurement for the proposed Project will be carried out in accordance with the World Bank's "Guidelines: Procurement of Goods, Works, and Non-Consulting Services under IBRD Loans and IDA Credits & Grants" dated January 2011, and "Guidelines: Selection and Employment of Consultants under IBRD Loans & IDA Credits & Grants by World Bank Borrowers dated January 2011, and the provisions stipulated in the Project's Legal Agreement. The various items under different expenditure categories are described 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 timeframe, are agreed between the Recipient and IBRD in the Procurement Plan. The Procurement Plan will be updated at least annually or as required to reflect the actual Project implementation needs and improvements in institutional capacity.

36. **Procurement of Works.** Works procured under the proposed Project will include the construction of facilities, roads and signals under Component 1, the construction and operation of final waste disposal Sites under Component 2, and civil works and facilities under Component 3. International Competitive Bidding (ICB) processes will be followed for all contracts estimated to cost US\$3,000,000 or above. Packages amounting to under US\$3,000,000 in the aggregate may be procured using National Competitive Bidding (NCB) processes. Shopping procedures may be used for contracts amounting up to US\$250,000. Procurement of works will be done using the Bank's standard bidding documents (SBD) for all ICB procurement. For NCB or Shopping (S) methods, documents agreed with or satisfactory to the Bank will be used. Works for the restoration and rehabilitation of monuments under "*Puesta en valor*" will be executed under the Force Account method, the procedures and the positive list of activities will be detailed in the OM. The concessionaire and contractor for the construction and operation of the final waste disposal sites will be selected under ICB, or, if duly justified, under Limited International Bidding (LIB). Standard bidding documents for the final waste disposal sites shall be deemed acceptable to the Bank.

37. **Procurement of Goods and Non Consultant Services.** Goods procured under the

proposed Project will include: Procurement of materials for works under Force Account (regional and commercial materials), computers, waste management equipment (trucks, vehicles, recipients, etc.), meteorological and communications equipment for the early alert systems. ICB processes will be followed for all contracts estimated to cost US\$250,000 or above. Packages amounting to under US\$250,000 in the aggregate may be procured using NCB processes. Shopping procedures may be used for contracts amounting up to US\$50,000. Procurement of goods and non-consultant services will be done using the Bank's SBD for all ICB procurement. For NCB or Shopping methods, documents agreed with or satisfactory to the Bank will be used.

38. All procurement notices shall be advertised in the Project's website, the government's website, and in at least one local newspaper of a wide national circulation. ICB notices and contract award information shall be advertised in the United Nations Development Business online (UNDB online), in accordance with provisions of paragraph 2.60 of the Procurement Guidelines.

39. **Selection of Consultants:** Consulting Firm services will be contracted under the proposed Project for the purposes of studies, supervision services, engineering, training, and logistics. The procurement of consulting firms will be carried out using the Bank's standard Request for Proposals (RFP). International firms will have the opportunity to participate in all solicitations above US\$300,000. Expression of interest or consultant services estimated to cost less than US\$350,000 per contract may be advertised only in Peru in accordance with the provisions of paragraph 2.7 of the Consultant Guidelines. Consulting Firms would be selected following Quality- and Cost-based Selection (QCBS) for all contracts in the estimated amount of more than US\$100,000.

40. **Selection of Individual Consultant Services.** Individual consultant services will be contracted mostly for project management and for technical advice, mainly in the substantive matters of the Project. The TORs, job descriptions, minimum qualifications, terms of employment, selection procedures, and the extent of Bank review and documents shall be described in the Project's OM and the contract shall be included in the Procurement Plan to be approved by the Bank. All the individual contracts procurement process shall be advertised in the Government website (www.copesco.gob.pe).

41. A Project website, a government website and a national newspaper shall be used to advertise expressions of interest as the basis for developing shortlists of consulting firms and individual consultants and to publish information on awarded contracts in accordance with the provisions of paragraph 2.31 of the Consultants' Guidelines and as mandated by local legislation. Contracts expected to cost more than US\$300,000 shall be advertised on UNDB online.

42. **Training.** Training will include expenditures (other than those for consultants' services) incurred by the Borrower to finance logistics for workshops, meetings, and seminars, and reasonable transportation costs and per diem of trainees and trainers (if applicable), training registration fees, and rental of training facilities and equipment. The procurement will be done using NCB and Shopping procedures as discussed below. Direct Contracting (paragraph 3.7 of

the Procurement Guidelines) may be used for the payment of registration fees, up to a ceiling amount to be established annually in the Procurement Plan.

43. **Operating Costs.**¹⁷ The Project will finance expenses for project administration. These expenses will include major Project operating costs, including hiring personnel and procuring hardware and software. These operating costs will be administered in accordance with the Bank's Procurement Guidelines, as appropriate. This procurement also will be carried out using the Bank's SBD or National SBD agreed with or satisfactory to the Bank.

B. Procurement Plan

44. The CRG has prepared a draft procurement plan for the first 18 months of Project implementation based on existing information and the envisaged implementation of the Project. This plan has been discussed and agreed upon between the Borrower and the Project Team at Appraisal and will be finalized during Negotiations and will be available at each office as well as in the Project's database and on the Bank's external website. The Procurement Plan will be updated semi-annually or as required by either the Borrower or the Bank to reflect the actual Project implementation needs and improvements in institutional capacity. The Procurement Plan will be available at the Procurement Plan Execution System (*Sistema de Ejecucion de Planes de Adquisiciones*, or SEPA).

45. The Procurement Plan shall set forth those contracts which shall be subject to the Bank's Prior Review. All other contracts shall be subject to Post Review by the Bank, except for those contracts terminated by the recipient's agency for which the Borrower shall seek the Bank's no objection prior to the proposed termination.

C. Frequency of Procurement Supervision

46. In addition to the prior review supervision to be carried out by Bank offices, the capacity assessment of COPESCO has recommended three to four procurement supervision missions per year for the first two years and two missions per year thereafter, including field visits, post-reviews of procurement actions. One in five contracts will be post-reviewed by the Bank. Based on the finding of the procurement post reviews and the proposed ratings, the Bank may determine the revision of the prior review requirements.

D. Details of the Procurement Arrangements Involving International Competition

1. Goods, Works, and Non Consulting Services

(a) List of contract packages to be procured following ICB and direct contracting:

¹⁷ Operational Costs. Expenses on account of project management and monitoring, including office supplies, utilities, rental, insurances, vehicles and equipment operation, transport, travel, per diems, supervision costs, and local contractual staff salaries but excluding salaries of officials of the Borrower's civil service, at the national and local levels, will be financed as operational costs and procured using shopping procedures, when possible, and the implementing agencies.

1	2	3	4	5	6	7	8	9
Ref. No.	Contract (Description)	Estimated Cost	Procurement Method	P-Q	Domestic Preference (yes/no)	Review by Bank (Prior/Post)	Expected Bid-Opening Date	Comments
1	Design, build and operate the waste disposal sites	20.000.000	ICB/LIB	No	No	Yes	May 5, 2014	
2	Procurement of waste management equipment	3.000.000	ICB	No	No	Yes	April 21, 2014	
3	Procurement of meteorological equipment	1.000.000	ICB	No	No	Yes	N/A	
4	Procurement of communications equipment	250.000	ICB	No	No	Yes	N/A	

(b) ICB contracts for **works** estimated to cost above US\$3.0 million and ICB contracts for **goods** estimated to cost above US\$250,000 per contract and all direct contracting will be subject to prior review by the Bank. Direct Contracting regardless of the amount, will be subject to prior review by the Bank.

2. Consulting Services

(a) List of consulting assignments with short-list of international firms.

1	2	3	4	5	6	7
Ref. No.	Description of Assignment	Estimated Cost US\$	Selection Method	Review by Bank (Prior/Post)	Expected Proposals Submission Date	Comments

1	2	3	4	5	6	7
Ref. No.	Description of Assignment	Estimated Cost US\$	Selection	Review by Bank (Prior/Post)	Expected Submission	Comments
1	Supervision services for the DBO waste disposal	2.000.000	QCBS	Yes	N/A	
2	Component 1. Summary of contracts that will be let under QCBS	N/A	QCBS	Yes	N/A	

(b) Consultancy services estimated to cost above US\$100,000 per contract and all single source selection of consultants (firms) will be subject to prior review by the Bank. Individual consultant services to cost US\$100,000 or above per contractor single source, regardless of the amount, will be subject to prior review by the Bank.

(c) Shortlists composed entirely of national consultants: Shortlists of consultants for services estimated to cost less than US\$350,000 equivalent per contract may be composed entirely of national consultants in accordance with the provisions of paragraph 2.7 of the Consultant Guidelines.

E. Thresholds for procurement methods and prior review

Expenditure Category	Contract Value (Threshold)(USD000)	Procurement Method	Bank Prior Review
1.Works	>3,000	ICB/LIB	All
	3,000>250	NCB	First two each year
	<250	Shopping (Price Comparison)	First two each year
	Regardless of value	DC.	All.
2.Goods	>250	ICB	All
	250>50	NCB	First two each year
	<50	Shopping	First two each year
	Regardless of value	DC.	All.
	>100	QCBS	All

3.Consultant Services	<100	QCBS,QBS,CQ, FBS,LCS (per Procurement Plan)	All TOR. Selection Process Reviewed twice yearly (Ex Post).
	Regardless of value	SSS	All contracts awarded under SSS.
4.Individual Consultants	>100	IC	All
	<100	IC	All TOR. Selection Process reviewed twice yearly (Ex Post). All contracts awarded under SSS, and key personnel
	Regardless of value	SSS	All contracts awarded Under SSS, and key personnel
Total value of contracts subject to prior review: US\$ (No information available)			

Notes: ICB: International Competitive Bidding; LIB: Limited International Bidding; NCB: National Competitive Bidding; DC: Direct Contracting; FA: Force Account; QCBS: Quality-Cost Based Selection; QBS: Quality Based Selection; FBS: Fixed Budget Selection; LCS: Least-Cost Selection; CQS: Consultant Qualification Based Selection; SSS: Sole Source Selection

F. The capacity assessment of the Implementing Agency recommended High Risk. In addition to the prior review supervision to be carried out from Bank offices, the capacity assessment of the implementing agency has recommended semi-annual supervision missions to visit the field to carry out post review of procurement actions. The size of the sample for post review will be not less than one in five contracts. The risk rating for this Project will be reassessed and revised once there is evidence that mitigating measures are in place.

Social

47. The Project will deliver important benefits to the inhabitants of the Cusco region. The investments in the solid waste management and disaster risk management components will satisfy important needs of the city of Cusco and communities in the Sacred Valley. The restoration of historic and cultural heritage sites, improved access and, in general, the enhancement of tourism infrastructure and services will increase economic opportunities for local people.

48. The civil works that will be carried out as part of the Project require land acquisition and, therefore, could have adverse impacts. The solid waste management component also involves the closure of existing dumpsites, which will affect waste pickers. These potential adverse impacts will be addressed with the management plans described below.

49. **Indigenous Peoples.** A Social Assessment has been carried out to evaluate the potential effects of the four project components on Indigenous Peoples.

- *Solid Waste Management.* Two of the landfills (Calca and Urubamba) will affect communities of Indigenous Peoples. The Calca landfill will require the acquisition of

community land and the Urubamba landfill will be built on land adjacent to community land. Indigenous Peoples Plans are being prepared for these subcomponents. The IPP for Urubamba was consulted on August 10, 2013, disclosed in country on August 15, 2013 and disclosed on the Bank's external website on August, 15 2013. The IPP for Calca has been consulted and approved by the community of Vista Alegre Yanahuaylla (same dates as Urubamba) and is in the process of being approved by Parcco, a community adjacent to the landfill area. COPESCO and Parcco leaders have held three meetings (July 5, 31, and September 27 of 2013), during which the community indicated their satisfaction with the terms of the subcomponent and the strategy, but manifested interest in visiting other sites where similar projects have been implemented before giving its final approval. COPESCO and Parcco leaders are working towards meeting this demand and confirming their final, formal support for the IPP.

- *Tourism Services and Disaster Risk Management.* The interventions planned in the Sacred Valley as part of Components 1 and 3 may affect communities of Indigenous Peoples. An Indigenous Peoples Planning Framework has been prepared to address potential adverse impacts on these communities and to maximize project benefits for them. COPESCO has also carried out adequate consultation processes for every project component in a transparent and open manner to ensure there is documented broad community support.

50. Involuntary Resettlement. The anticipated impacts of land acquisition for subcomponents are as follows:

- *Solid Waste Management.* One of the three landfills (Urubamba) will be built on municipal land. The other two (Cusco and Calca) require land acquisition. The land for the Cusco landfill will be acquired from an individual and the land for the Calca landfill will be acquired from an indigenous community. Abbreviated Resettlement Plans have been prepared for the landfills of Cusco and Calca.
- The solid waste component will cause economic displacement among informal waste pickers. The closure of the waste dump in Cusco will affect the livelihoods of approximately 45 waste pickers. In addition, the changes in solid waste collection and disposal practices (including recycling) in the city of Cusco could affect the livelihoods of approximately 600 waste pickers. A Social Inclusion Plan has been prepared to address these impacts.
- *Tourism Services and Disaster Risk Management.* The interventions planned in the Sacred Valley as part of these components may require land acquisition. A Resettlement Policy Framework has been prepared to guide the preparation of resettlement plans during project implementation.

Environmental

51. The Project is classified as Category A under OP/BP 4.01 based upon the one moderately-sized landfill in Cusco (part of Component 2), even though this landfill is expected to improve the environmental sustainability of solid waste management in the region. The works associated with Components 1 and 3 involve relatively standard smaller-scale infrastructure works with potential environmental and social impacts that have been assessed as short-term, not significant, and can readily be prevented or mitigated with standard measures. The potential positive long-term impacts include: improving the quality and coverage of tourism services and

thus increasing the positive economic and social impacts in the Sacred Valley and surrounding areas; improving local capacity to efficiently collect, transport and dispose of solid waste, thus reducing environmental health impacts and promoting sustainable development; the appropriate closing and clean-up of existing informal dumpsites, thus removing potential focus of infections and environmental degradation; and helping to protect the local population, tourists, and infrastructure in touristic areas with high vulnerability to natural disasters. There are no anticipated significant negative indirect or long-term impacts related to the Project.

52. Related to Components 1 and 3, an ESMF has been developed. The ESMF includes an Indigenous Peoples Planning Framework and a Resettlement Policy Framework. Related to Component 2, an ESIA has been carried out for each of the three landfills each including an ESMP. The ESIA for the Calca and Urubamba landfills also include an Indigenous Peoples Plan, while the ESIA for the Cusco and Calca landfills include an Abbreviated Resettlement Plan.

53. For Component 1, an ESMF has been developed. The main potential environmental impacts would likely be due to the construction works associated with rehabilitation of existing roads to existing tourism sites, which are not anticipated to cause significant environmental impacts. Other potential impacts relate to works that will be within or near existing archeological sites. However, there are strong Peruvian regulatory procedures and oversight related to any such works, such as the presence of an archeologist/architect during works and continuous monitoring and reporting to the Ministry of Culture. The ESMF also contains relevant requirements.

54. For Component 2, an ESIA has been developed for each of the three landfills (Cusco, Calca and Urubamba). Each ESIA addresses environmental and social impacts, risks, and benefits, and includes an ESMP. An analysis of alternatives related to the best technology to apply to waste disposal (e.g., several local landfills, a regional landfill, and other combinations, including transfer stations) was conducted for Component 2. A site selection analysis was also performed for each landfill including various technical, environmental and social factors (e.g., critical or sensitive natural habitats, forests, proximity to populated areas or to environmental designated protected areas), and included stakeholder input.

55. Various potential negative environmental impacts and risks will be prevented or mitigated by the use of strong technical landfill design and operation standards and procedures. Construction environmental impacts are considered to be relatively low and easily mitigated with standard mitigation measures. Potential adverse impacts during operation include odors to neighboring communities, visual impacts, truck traffic and increased noise due to waste transportation, contamination of waters caused by leachate, slope erosion due to cuts in the terrain, and security risks such as gas accumulation in the new landfills. The Project does not involve the purchase or use of significant quantities of pesticides. However, the Project may involve the relatively minor use of pesticides during the operation of the landfills to control vectors (rodents, insects). The relevant ESMPs include applicable good practice procedures for pesticide use and storage, and prohibit use of pesticides excluded under OP 4.09. In terms of existing waste disposal sites, these will be either closed (e.g., Cusco and Calca) or the waste will be relocated to the new facilities (e.g., several small waste sites in the Sacred Valley). The closure will only happen once the new landfills are operational. Some potential but relatively

minor environmental impacts exist during the closure works such as release of waste and worker exposure.

56. For Component 3, an ESMF has been developed and consolidated with the ESMF for Component 1. The main potential environment impacts would likely be due to construction works that may occur in stream or river banks, which are relatively small in size and nature, and are not anticipated to cause significant environmental impacts.

57. The Project does not contemplate any significant negative impact on physical cultural resources. The ESIA's for Component 2 landfills have not identified any potential likelihood of encountering physical cultural resources. However, several of the activities for Components 1 and 3 might take place near or directly within the limits of archeological sites such as Ollantaytambo, which was declared National Cultural Patrimony in 2002. For these reasons, and given the sensitive social and cultural heritage context of the project area, the policy is triggered. Any environmental analyses, as part of the ESMF, associated with Component 1 and 3 subcomponents will specifically include consideration of physical cultural resources. All project ESMP and related construction contracts will include procedures and requirements related to chance find management. In addition, every activity carried out within an archeological site, by Peruvian law, will require the constant presence of an archeologist/architect designed by the Ministry of Culture.

58. The Project does not support the construction or rehabilitation of dams. However, as part of Component 3 there may be disaster risk management works in two stream or river basins that have existing relatively small reservoirs located in their headwaters. The ESMF for Component 3 includes specific measures to assess any relevant existing reservoir and to take appropriate actions, as deemed warranted, consistent with OP 4.37.

59. COPESCO will be responsible for project implementation and the PCU will be responsible for overall Project administration, including social and environmental management. The PCU has staff and experience related to Bank safeguards (e.g., the previous Vilcanota project and trust funds for project preparation). The Component 2 works may be contracted as design-build and/or operate contracts, require compliance with the specific landfill ESMP, and will have supervision which will include environmental and social aspects. The execution of works in Components 1 and 3 will be contracted to construction companies, who will be required to comply with the environmental and social requirements developed under the ESMF and any applicable Peruvian regulatory requirements including those related to culture heritage. Supervision of these works and activities will be contracted to consultants, who, in addition to technical supervision, will provide environmental and social supervision. The Project's OM will include relevant environmental and social aspects, including compliance with project ESMF and social management plans (Indigenous Peoples Plans and Resettlement Plans), environmental and social conditions in project contracts, use of supervisors for project contracts, and supervision responsibilities of COPESCO.

60. There has been steady process during project preparation to keep stakeholders informed and to receive input related to the Project. Starting in 2011, the CRG, through COPESCO, has been leading a number of activities aimed at explaining the project's scope, objective, main

anticipated impacts and mitigation measures. Conversations and workshops have taken place directly through COPESCO or through the consulting firms in charge of preparing designs and environmental and social studies. Technical working groups were also created, to which updates on project preparation were provided and from which feedback was sought. As part of the development of the ESIAs for the three landfills, consultation was performed with stakeholders to help define potential issues and alternatives. An initial draft ESIA for the Cusco landfill was disclosed to the public on December 2012 and a revised draft in July 2013. The draft ESIAs for Calca and Urubamba were publically disclosed in July 2013. The three ESIAs were consulted with various local communities (e.g., Huancabamba (Cusco), Yanahuaylla (Calca), Paca Huaynacolqa (Urubamba), during June and July 2013. Additionally, during July 2013, consultations were held with municipality personnel, representative governmental and civil society institutions, and other rural communities. The principal comments from the consultations included: not to repeat the history of the current management of waste in landfills (i.e., relatively poor management), concerns about the potential risks of water pollution and health risks for persons living near the new landfills, operation/effectiveness of landfill geomembranes as a barrier to protect/prevent contamination, employment opportunities in the construction and operational phases of the project, suggestions for expanding descriptive information about fauna, flora, social aspects, and application of other benefits to surrounding communities. The ESMF was disclosed and consulted in August 2013.

Monitoring & Evaluation

61. The results framework, presented in Annex 1, has been developed in close coordination with COPESCO, and will be carried out by the PCU. The PCU will consolidate data at the project level and produce semi-annual reports to monitor progress. A beneficiary survey will analyze the effect of the planned tourism investments on improving the quality of service delivery in the Project area.

62. Overall responsibility for monitoring and evaluation of the Project will lie with the PCU, which will provide timely information about the Project's implementation progress, including qualitative information on the execution of selected activities, procurement and contractual decisions, accounting and financial recording, and other operational and administrative matters. The Project will support capacity building and development of a monitoring and evaluation system, as COPESCO does not have a consolidated monitoring and evaluation system in place. The Project's OM will provide specific details regarding monitoring and evaluation responsibilities, including data collection requirements, timing and use of information.

Annex 4: Operational Risk Assessment Framework (ORAF)

Peru: Cusco Regional Development (P117318)

Project Stakeholder Risks						
Stakeholder Risk	Rating	Moderate				
<p>Risk Description:</p> <p>A diverse set of stakeholders are involved in the Project. The CRG, local municipalities and the central government are active players that need to work in close collaboration. Additionally, several specialized agencies, such as the Department of Culture and the Department of the Environment, will be involved during implementation of the different activities. The complexity in the roles, responsibilities and relationships among the multiple institutions might delay Project’s implementation.</p> <p>Due to the characteristics of the Project (i.e., solid waste disposal) and the Project’s area in terms of unique cultural and environmental context, CSOs as well as the local population’s support are key to achieve the PDO. In view of past experiences during the PRRVV implementation, there is a risk of opposition or lack of support, primarily for the solid waste component, that may affect the Project’s implementation.</p>	<p>Risk Management:</p> <p>The CRG is aligned with the central government and shares common goals for their mandates. All investments will benefit municipalities in a significant way and are priorities of the CRG’s development strategy. A stakeholder mapping and institutional assessment for the Project has been carried out to delineate roles and responsibilities of key actors. In addition, the CRG has prepared a draft Memorandum of Understanding with the Department of Culture.</p> <p>To ensure broad support for the Project, the CRG has been working with communities in project areas to explain project benefits to raise awareness, build support for the investments, and negotiate other means of support, including economic development, basic service provision, and improved road access.</p>					
	Resp: Client	Status: In Progress	Stage: Both	Recurrent: <input type="checkbox"/>	Due Date: 31-Dec-2013	Frequency:
Implementing Agency (IA) Risks (including Fiduciary Risks)						
Capacity	Rating	High				
<p>Risk Description:</p> <p>COPESCO’s capacity to bid out infrastructure contracts, manage and administer contracts and financial matters is a potential risk.</p>	<p>Risk Management:</p> <p>COPESCO, which is part of the CRG, has experience executing World Bank-financed projects, including in the procurement of civil works and the engagement of consultants. The key fiduciary, social, environmental and technical staff members who</p>					

Project implementation may be affected by the administrative, human resource and fiduciary capacity of the Project’s implementing agency.	are experienced and had satisfactory performance from the previous project are programmed to work for the proposed Project and are being supplemented with additional staff. This core team is responsible for the preparation and implementation tasks of the Project. Based on the results of the fiduciary and safeguards capacity review of COPESCO conducted by the Bank, a support strategy and capacity strengthening measures will be implemented.					
	COPESCO also has agreed to develop its in-house technical capacity and to be held accountable for technical quality of contracted activities and to actively oversee the supervision firms.					
	Resp:	Status:	Stage:	Recurrent:	Due Date:	Frequency:
	Both	In Progress	Both	<input type="checkbox"/>	31-Dec-2013	
Governance	Rating	Moderate				
Risk Description:	Risk Management:					
The Project will be the first Bank-financed operation prepared by a regional government in Peru.	An institutional assessment has been carried out by COPESCO as part of project preparation. The assessment delineates roles and responsibilities of different agencies at the national and regional level. Given implementation will occur at the regional level, the creation of the Project Coordination Committee will help enhance coordination and communication across stakeholders and reduce the risk of overlapping roles and responsibilities. The Technical Working Groups are also being put in place per component. These Working Groups will operationalize the decisions reached at the Coordination Committee level and to make sure the municipalities and technical staff are fully engaged in the implementation process, as these stakeholders will eventually be responsible for operations and maintenance of assets financed under the Project.					
Peru has been recently decentralized, and the CRG does not have much experience in coordinating with the multiple municipalities involved in the Project. Lack of a shared strategy and overlapping responsibilities among institutions may occur.						
Additionally, it is important to ensure transparency in sharing of information about the Project.	The team will work closely with the Government to establish transparency in sharing information, including advertising of contracts and dissemination of information about the Project. COPESCO currently posts key documents on its website and is developing a communications strategy for the Project. Institutional arrangements include a Communications Specialist as part of the PCU to support open information access and dissemination.					
	Resp:	Status:	Stage:	Recurrent:	Due Date:	Frequency:

	Client	In Progress	Both	<input type="checkbox"/>	30-Jun-2014	
	Risk Management: <p>As a preventive measure, the task team will provide close supervision support on procurement and FM. The Project's bank account will be regularly audited and transparency in Project implementation will be ensured through disclosure of the Project's OM, Progress reports, procurement plan and other relevant documents. Audits under the previous project did not have major findings.</p> <p>The design of the fondo concursable will bear in mind the need to mitigate risks of fraud and corruption; a disbursement condition for the initiation of use of funds for technical assistance to be provided to beneficiaries will be put in place to ensure the Bank is satisfied with the design prior to the implementation of the pilot. In addition, the fund will have its own OM that will include explicit measures to minimize incidences of fraud and corruption.</p>					
	Resp: Bank	Status: Not yet due	Stage: Supervision	Recurrent: <input type="checkbox"/>	Due Date: 31-Jan-2014	Frequency:
Project Risks						
Design	Rating	High				
Risk Description: <p>Given past experience in securing MEF approval for specific infrastructure investments within the National Public Investment System (SNIP), there is a risk that the preparation of some components may be delayed.</p> <p>Land acquisition for the Cusco and Calca landfills is still pending. If the land is not successfully acquired, the solid waste component will not be viable.</p>		Risk Management: <p>Preparation of infrastructure investments is already underway, with most investments well-defined; the disaster risk management investments are the ones still in the process of being defined. MEF sector specialists have been active in project preparation from an early stage, and several visits to Cusco have taken place during project preparation. In addition, the CRG and the MEF are committed to finalizing remaining activities and investments in a timely manner to ensure investments are sound and meet the Project's objectives.</p> <p>In Cusco and Calca, COPESCO has received documentation indicating the land owner/community's commitment to sell the land. Negotiations are underway to determine the final price of the land in each case. COPESCO has no reason to believe the sale will not take place and can only proceed with the sale once the Project is approved. As a mitigation measure, the Bank is making the sale of the land a condition for bidding for the landfill works. Also, the Bank has triggered OP 4.12,</p>				

	cautiously considering the land acquisition as involuntary, although it is believed to be voluntary. This will ensure Bank standards are complied with in the unlikely event of expropriation.					
	Resp: Client	Status: In Progress	Stage: Both	Recurrent: <input type="checkbox"/>	Due Date: 31-Jan-2014	Frequency:
Social and Environmental	Rating	High				
Risk Description: Potential environmental and social impacts associated with the solid waste management component, including the economic displacement of waste pickers. The closure of the existing dumpsite in Cusco may not be carried out in an acceptable manner and may not adequately address affected communities. The Project area has significant historic and cultural heritage resources, and some of the activities for Components 1 and 3 might take place near or directly within the limits of archaeological sites such as Ollantaytambo (which was declared National Cultural Patrimony in 2002).	Risk Management: An ESIA has been developed for each of the three landfills, each including an ESMP. An analysis of alternatives related to the waste management technology and site selection analysis for each landfill was performed. Various potential negative environmental impacts and risks will be prevented or mitigated by the use of strong technical landfill design and operation standards and procedures. The Cusco Regional Government, through COPESCO, has implemented stakeholder participation measures and is supporting the establishment of effective grievance redressal mechanisms. A Social Inclusion Plan will be implemented to assist waste pickers in their efforts to restore their income and livelihoods. The Project will provide technical assistance to the Province of Cusco to support the closure of the existing dumpsite. In addition, communities adjacent to the existing dumpsite and new landfill in Cusco will be included in the Social Inclusion Plan. Appropriate procedures will also be included in the OM to support COPESCO's ability to monitor progress on the closure. The ESMF for Components 1 and 3 includes consideration and measures related to physical cultural resources. All subcomponents will include procedures and requirements related to chance find management. In addition, every activity carried out within an archaeological site, by Peruvian law, will require the constant presence of an archaeologist/architect in coordination with the Ministry of Culture. None of the three landfills proposed under Component 2 will be implemented in the vicinity of any known archaeological site.					
	Resp: Client	Status: In Progress	Stage: Both	Recurrent: <input type="checkbox"/>	Due Date: 31-Dec-2017	Frequency:

Program and Donor	Rating	Low				
Risk Description: There are no other donors involved in this Project.	Risk Management:					
	Resp:	Status:	Stage:	Recurrent:	Due Date:	Frequency:
				<input type="checkbox"/>		
Delivery Monitoring and Sustainability	Rating	High				
Risk Description: Local capacity to maintain Project initiatives after Project completion is weak. The proposed Project has garnered the support of the President of the CRG, as well as the mayors of the municipalities participating in the Project. However, elections will take place in 2014 and if the political leadership changes, priorities could shift to other development issues. The maintenance and sustainability of the solid waste system still needs to be defined. A large amount of counterpart funding is linked to the Project and the Government may not be able to afford counterpart funding in later years, given the political cycle mentioned above.	Risk Management:					
	Feasibility studies for each investment have considered financial sustainability and a system will be put in place to ensure sufficient resources for maintenance of investments and other Project initiatives.					
	Political risk is being mitigated through broad consultation with a range of stakeholders at the regional and municipal level to ensure ownership and sustainability of investments beyond the political cycle.					
	During the roll out of the new solid waste management systems, cost recovery will be addressed in parallel with infrastructure investments in order to fundamentally change the cost recovery ratio during this period. The Bank has worked with the CRG and MEF to prepare a financial analysis of the Project to review affordability of the loan and counterpart funding required for the Project and found the CRG has the carrying capacity to implement the Project. Counterpart funds noted in the Loan Agreement are obligatory for incoming administrations to comply with and finance.					
	Resp:	Status:	Stage:	Recurrent:	Due Date:	Frequency:
	Both	In Progress	Both	<input type="checkbox"/>	31-Dec-2014	
Overall Risk						
Overall Implementation Risk:	Rating	High				
Risk Description:						
The main risks during implementation include the lack of coordination across line ministries and agencies at the regional level, the adequate closure of the existing dumpsite in Cusco, the ability to maintain political and community support for the Project, and weak capacity within COPESCO to implement the Project. These risks and corresponding mitigation measures will be closely monitored during implementation.						

Annex 5: Implementation Support Plan

PERU: Cusco Regional Development Project

Strategy and Approach for Implementation Support

1. The Implementation Support Strategy design draws upon the risk profile of the Operational Risk Assessment Framework (ORAF, Annex 4) and aims to enhance the client's quality of delivery of the proposed investments. This strategy is focused on risk mitigation measures as per the ORAF and regular Bank implementation support, including technical, institutional, social and environmental safeguards, and fiduciary aspects.

2. The proposed Implementation Support Strategy includes the following main elements:

- a) The Project will be supervised by a headquarters-based team which will coordinate with the Country Office in Lima as necessary.
- b) Implementation support will start immediately after Board Approval to finalize and initiate the procurement of the Project's key activities. Frequency of supervision missions is expected to be higher at the beginning of implementation (possibly up to four per year) and decrease to the usual two to three missions per year after the Project reaches a good implementation pace.
- c) Fiduciary and safeguards trainings will be provided early on to the CRG's implementation staff and the Bank's fiduciary and safeguards staff will initially provide support and advice to their counterparts in addition to their implementation support function.
- d) The Implementation Support Plan will be revised regularly on the basis of project progress and continuous risk assessment.

Implementation Support Plan

3. **Technical Support.** Most of the investments contemplated under the Project are not technically highly complex. Rather, the complexity lies in the inter-institutional arrangements that require coordination in order to implement the Project's activities. Specifically:

- a) *Component 1.* The tourism component is large with numerous investments in a variety of locations of great cultural importance. Supervision of the works will require that the Bank's team have solid technical experience regarding infrastructure and the tourism sector, especially during the first two years of project implementation. In addition, specialized technical expertise will be required to support the design and roll-out of the Competitive Fund for Tourism (*Fondo Concurable*) during implementation.

- b) *Component 2.* The solid waste component will include a combination of well-planned institutional responsibilities and technical assistance and capacity building as part of the component. Key issues to be addressed include provision of technical assistance to the Regional Government during the bidding process and in solid waste contract oversight, which will be especially critical in the event a design-build-operate contract is utilized, capacity building for the local government in operation and supervision, policy support including support to revenue generation and capacity support in the implementation of the Social Inclusion Plan for waste pickers.
- c) *Component 3.* The disaster risk management component requires technical expertise in implementing early warning systems and in providing guidance for the preparation and implementation of disaster risk management plans for the region. This component will need to be supported by an experienced disaster risk management specialist throughout the Project.

4. **Fiduciary support.** As previously mentioned, the CRG has previously implemented a Bank-funded project (PRRVV) and trust fund activities through COPESCO. As a result of the fiduciary assessment, an action plan has been suggested on both FM and procurement in addition to closer initial supervision needs. Specifically:

- a) *Procurement:* The Bank supervision team will: (i) Provide training to the Project staff at the CGR and COPESCO; (ii) provide advice and support to the Procurement Specialists in the PCU; (iii) review procurement documents and provide timely feedback to the PCU; and (iv) monitor procurement progress against the Procurement Plan.
- b) *Financial Management:* FM supervision would include on-site and off-site supervisions. On-site supervision missions will be carried out at least twice a year to the extent possible during the first year and later calibrated to once a year. Off-site supervisions will comprise desk reviews of interim financial reports and audited financial statements. Additionally, COPESCO will benefit from fiduciary training and technical assistance from the Bank.

5. **Safeguards support.** Given the Project components and works, specifically three new landfills and various subcomponents in Components 1 and 3, which will need to be processed according to the ESMF, strong and regular safeguards support for implementation will be important throughout project implementation. Support for addressing land acquisition issues and economic displacement is required for the solid waste components and possibly for the tourism and disaster risk investments.

6. **Implementation main focus.** The following table summarizes the main focus of implementation during the life of the Project.

Time	Focus	Skills Needed	Resource Estimate	Partner Role
First twelve months	Getting the Project underway and generating goodwill With early results	Project management, technical support in infrastructure, solid waste, disaster risk management and safeguards	150 percent of supervision budget	Begin infrastructure works related to tourism, solid waste, development of Competitive Fund for Tourism and disaster risk management activities
12-48months	Developing good practices, implementing activities	Project management, technical support in infrastructure, solid waste, disaster risk management and safeguards	Normal supervision budget	Improve speed and efficiency of implementation of all three components
Closing	Drawing lessons learned	Project management, monitoring and evaluation	Normal supervision budget	Complete works and activities

Skills Mix Required

9. The following table summarizes the proposed skill mix and number of staff weeks in the initial phase of project implementation. It is expected that demand will decrease and change with time.

Skills Needed	Number of Staff Weeks	Number of Trips	Comments
Task Team Leader	8	2-3	headquarters-based
Sector Specialist (Urban/Cultural Heritage)	10	4-6	Two people
Environmental Specialist	4	2	Two people
Social Specialist	4	4	Two people
Procurement Specialist	8	4	Two people (first two years)
Financial Management Specialist	2	1	
Disbursement Specialist	2	0	
Solid Waste Management Specialist	4	2-4	
Disaster Risk Management Specialist	4	2-4	
Communications Specialist	4	4	
Operations Analyst	4	2-4	

Partners

Name	Institution/Country	Role
Client	MEF	Borrower
PCU	CRG/ COPESCO	Implementing Agency
Project Partner Institutions	Ministry of Culture, Ministry of Environment, Ministry of Tourism , Provinces and corresponding Municipalities and Districts of Calca, Urubamba and Cusco	Each partner has its own roles/responsibilities for specific activities under the Project.

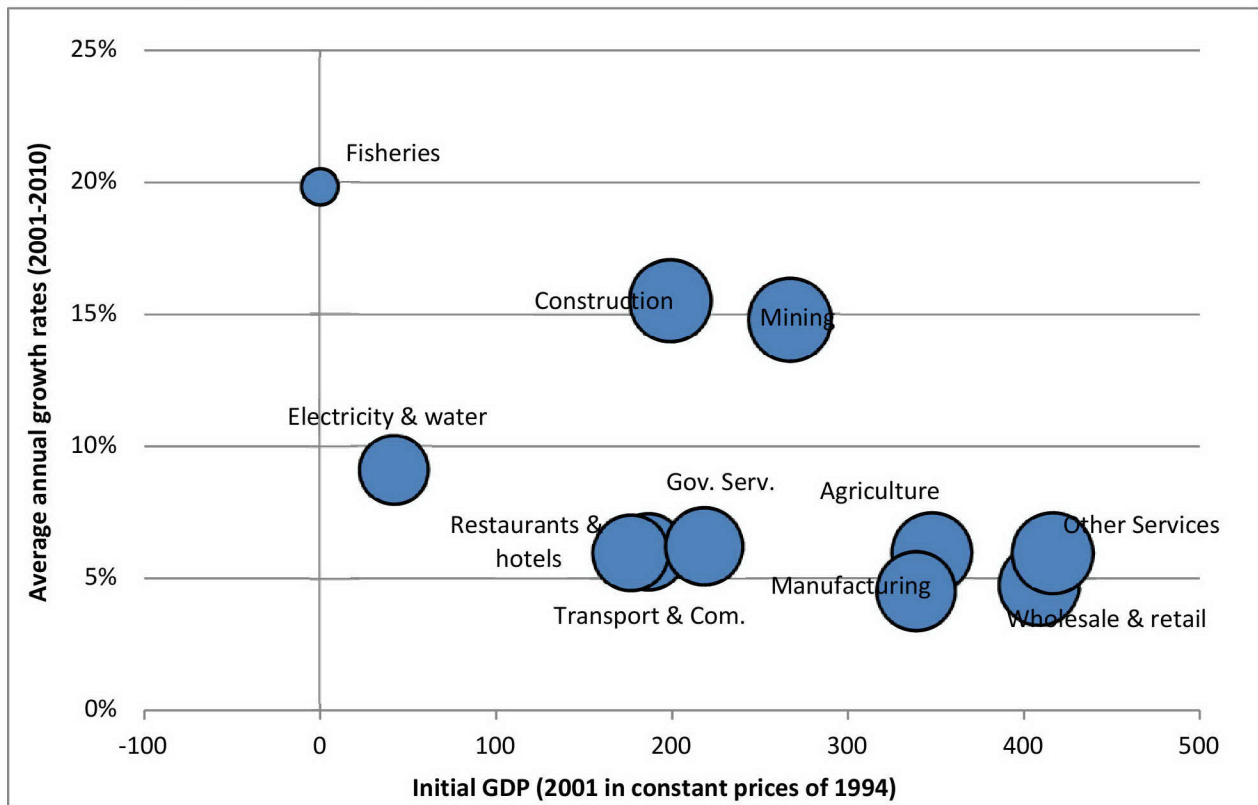
Annex 6: Economic and Financial Analysis

PERU: Cusco Regional Development Project

Cusco's performance and changing economic structure

1. Cusco has grown impressively over the past decade, achieving the best performance among all Peruvian departments. The region more than doubled its economic size in only 10 years, going from 2.6 billion *nuevos soles* (US\$930 million) to more than 6 billion (4,696 *nuevos soles*, US\$2.15 million in per capita terms). The region therefore, grew at an average annual rate of 7.4 percent, the fastest economic expansion among all Peruvian departments in the period. Although the strongest sectoral performance in Cusco –at an average annual growth rate of nearly 20 percent – took place in fisheries (Figure 4), almost 50 percent of economic growth was due to mining (27 percent of regional growth during the period) and construction (22 percent of that regional growth). Despite the fact that Cusco is one of the top destinations for tourists not only in Peru, but in the continent, tourism-related activities such as transport, restaurants and hotels, as well as other services had significant annual growth rates, albeit not in comparison with other industries.

Figure 4. Cusco's Regional Economic Structure and Growth (2001-10)



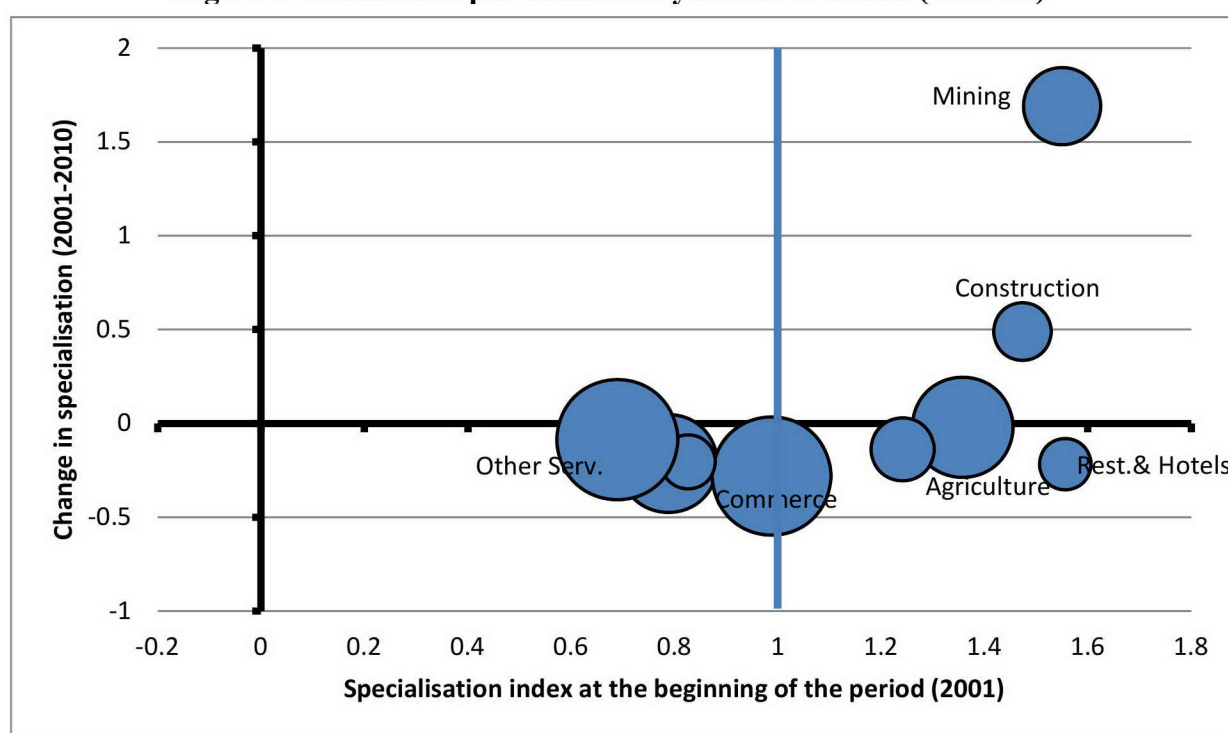
Source: Own calculations based on INEI (2013)

2. Cusco has also quickly transformed into a mining region while other industries might not be evolving as rapidly as those same activities elsewhere in Peru. In 2001, Cusco was specialized

in agriculture, mining, construction, restaurants and hotels and government services (Figure 5). That is, those activities had a relatively stronger presence in the region than at the national level.¹⁸ By 2010, the region had only further specialized in three industries: mining, construction and electricity and water. In particular, Cusco's specialization in mining activities grew significantly in just 9 years.

3. It is surprising that activities traditionally related to tourism activities such as lodging and catering (represented in Figures 4 and 5 as restaurants and hotels), transport or commerce have actually declined in specialization despite its steady economic growth. These results may signal a lower than national average level of growth in these industries. With Machu Picchu and the Sacred Valley increasingly attracting tourists, the economic gains might be positive, but other regions might be reaping greater benefits than Cusco.

Figure 5. Industrial Specialization Dynamics in Cusco (2001-10)



Source: Own calculations based on INEI (2013)

4. The new economic structure geared to typically capital-intensive activities in mining, opens up a discussion of what to do to spur wages and employment in labor-intensive local activities in Cusco. The proposed Project has the benefit of contributing to increasing direct economic benefits for firms and individuals directly linked to an increased number of tourists, their length of stay and their spending. It also contemplates the multiplier effects that such a demand would place on inputs to service providers in the tourism sector. The Project therefore, is

¹⁸This initial condition can be seen in Figure 5 to the right of the blue line. The line establishes the value of 1 for the specialization index calculated as a quotient of the region's sectoral GDP to the industries at the national level, such a quotient is then corrected by the regional share of national GDP.

conceived in a way that the entire regional economic system is taken into account and not only those directly in contact with tourists.

5. Although we tend to think of tourism as a destination activity, it is actually a global value chain. Outbound countries participate with tourists' demand for international distribution services such as those that can be delivered by a travel agency or a tour operator, as well as for international transportation such as an international air carrier. Inbound countries can benefit from demand on national distribution (e.g. national tour operator), national transportation not only through national air carriers, but also through ground transportation services. In addition, recipient countries benefit also from accommodation and excursion (Table A6.1).

Table A6.1: Global Value Chain in Tourism

Outbound country		Inbound country			
International distribution	International transport	National distribution	National transport	Accommodation	Excursions
Travel agent	International air carrier	National travel agent	National air carriers	Luxury hotels	Activities
Tour operator	Cruise	National tour operator	Ground transportation services	Large hotels	Local guides
Global distribution systems		Local tour operator		Small hotels	National parks, monuments
Independent		Destination management organization			Retail, Restaurants

Source: Christian, M. (2013) "Global Value Chains, Economic Upgrading and Gender in the Tourism Industry" in C. Staritz and J.G. Reis (eds.) *Global Value Chains, Economic Upgrading and Gender: Case Studies of the Horticulture, Tourism, and Call Center Industries*, World Bank.

6. The value chain for Cusco's tourism industry is therefore, not only related to distribution, transportation, accommodation and excursions, but also to the activities that provide support to these. As a consequence a broader value chain takes into account employment in distribution and transport, as well as services related to maintenance of vehicles that provide such transport. In addition, the value chain is completed by employment and sales for activities that provide catering, accommodation, entertainment and artisanal products. Many of these activities are performed locally and so the benefits for the community are expected to be localized.

7. Ensuring that those benefits provided by tourism are embedded locally and do not discriminate by gender or ethnicity is key to accruing the social returns of investing in tourism. The UN World Trade Organization (2011) report shows that female employment in tourism is concentrated chiefly on the accommodation and excursion segments of the value chain. In Latin America, almost 60 percent of employment in accommodation is women. However, these women typically perform activities that require low to mid-level skills such as housekeeping,

laundry, catering or clerical work (Christian, 2013). Women are also typically relegated to jobs that can provide flexibility so that they can perform both, their family's household work and casual work as artisans, retail vendors or wait staff in family restaurants. Women also endure a persistent global wage inequality in tourism with a gap that ranges from 10 to 15 percent less earnings than their male counterparts. Practices imposed by global demand to reduce prices, or as a result of marketing an image, can have serious consequences on the lack of opportunities and wage inequality for women in the destination country. In addition, in many developing countries, women have fewer opportunities to train themselves in the tourism industry than men. Finding ways to ensure that women have equal training and job opportunities is therefore key to upholding the social benefits of the Project. A similar argument can be made for ethnic minorities that are typically the ones providing excursion and artisanal work requiring equal opportunities.

Financial Sustainability: Multiplier Effects

Methodology and assumptions

8. Although tourism is an economic activity that cannot be associated with one single sector, the positive effects of it cannot only be associated to foreign currency growth influencing the country's balance of payments, but also to economic growth (GDP), as well as an income redistribution mechanism and to other indirect benefits resulting from the multiplier effects of visitors' spending. Direct benefits of tourism activities are those associated with the payments to the factors of production most intimately related to the provision of goods and services to tourists. Indirect benefits result from increased demand for goods and services in the production chain that can trickle down in the economy becoming a multiplier effect. Both direct and indirect benefits are not only those related to transactions in a productive chain, but also the payments to the factors of production such as labor. We can distinguish, therefore, between direct labor that results directly as a consequence of the payments made by tourists, indirect employment that takes place along the production chain, and induced employment that results from the spending made by residents' earnings in tourist activities.

9. Following this approach of direct and indirect benefits, the evaluation of the benefits and costs of this Project was carried out by making social returns on tourism a function of tourists' spending. In turn, the latter is a function of daily spending by tourists, the size of demand (number of tourists) and the nights spent in the region. The evaluation also estimated the number of individuals that depend on tourists' income, the cost of the touristic product, the capacity of the services plant and the capacity to accommodate tourists (both making up the size of the supply). The evaluation made an explicit estimation of the benefits with and without the Project so that a net benefit of the Project could be identified. Such differential of benefits stems from the estimation of the current benefits as a baseline scenario and the projected benefits taking into account the aforementioned factors to determine the likely increase in the number of tourists and their spending. It is important to mention that the estimated benefits under moderate and conservative scenarios are both reasonable and modest given the fact that the calculations exclude the expanded benefits from the likely growth in supply as a result of an increase in demand.

10. The estimations made separate calculations for foreign and domestic tourists. To estimate the former, the calculations assumed that foreign and domestic tourists alike have an untapped consumer surplus. By extending the number of nights that a tourist spends in the region, a greater proportion of that surplus can be seized. In addition to the number of nights, the Project assumes an increase in the number of tourists coming to the region and rising daily spending. The following projections assumed that without the Project, under a baseline scenario, there would be a total annual rise in demand (number of tourists) of 7.18 percent with foreigners being slightly more interested at 7.27 percent than domestic ones (7.02 percent). The projections make the same annual increase assumption in demand, but it also allowed for growth in demand to peak twice during the project life. In 2017, projections estimate an increase of 31.75 percent with respect to the previous year; in 2021, projections assume an increase of 28.7 percent with respect to 2020. Given that investments are taking place until 2017, net benefits in terms of number of tourists between the Project and the baseline scenario are assumed to be null, but they start picking up that year. Total spending by tourists was estimated assuming that they will be willing to increase their stay from one day to two.

11. Other direct benefits in the form of funds to strengthen local firms providing goods and services for the industry were estimated by assuming an increase in funds available for entrepreneurs in three different categories (touristic firms, artisan producers, and cultural industries) in 8 million *nuevos soles* (US\$2.86 million) each (except for the cultural industries, which is estimated at 3 million *nuevos soles*, US\$1.07 million). Since the funds require the beneficiary to contribute with 20 percent of investment, total investments are estimated at 18.3 million *nuevos soles* (US\$6.55 million). Under the moderate scenario, a rate of return of 15 percent was assumed for touristic firms' projects, a 12 percent return was assumed for the other two types of funds, whereas under the conservative scenario, rates of return are adjusted down to 12 percent and 10 percent respectively. The multiplier effect was calculated to yield private benefits at nearly 2.5 million *nuevos soles* (US\$894,295) under the moderate scenario and 2.025 million *nuevos soles* (US\$724,378) under a conservative scenario. Social benefits of those private returns were adjusted using a correction factor of 0.8475.

12. Estimates run on the financial sustainability of the Project projected that the national multiplier of the Project for accommodation and catering would stand at 1.446 which means that for every *nuevo sol* (US\$0.36) of augmented spending due to the Project, national GDP would increase by 1.446 *nuevos soles* (US\$0.52). Multiplier effects estimates rest on the assumption that indirect impacts on diverse value chains linked to an increased tourism offer and the demand for goods and services that would be associated with it.

13. The Project's total impact over its 12-year life period will approach 3 billion *nuevos soles* (US\$1.07 billion). Sectoral impacts, based on an input-output matrix approach,¹⁹ can be identified in Table A6.1.

¹⁹ An input-output matrix approach can be as useful as reliable are the coefficients used in its construction. Coefficients are therefore calculated on the basis of past transactions and extrapolated to the corresponding year. The usual assumptions on building such coefficients were made. First, inter-temporal homogeneous technologies that imply no technological change. Such assumption can be restrictive for some sectors that experience not only rapid technological progress, but where no unique production process can be identified. Second, the usual critique for this methodology also rests on the level of aggregation. However, disaggregating sectors to lower levels of activity could also unnecessarily increase the level of planning complexity.

Table A6.1. Total Sectoral Impacts of the Project

Sector	Total Impact (<i>nuevos soles</i>)	Sector	Total Impact (<i>nuevos soles</i>)
01.- Agriculture	167,851,742.610	24.- Non-metallic minerals	17,508,336.889
02.- Fisheries	6,551,277.682	25.- Steel	8,278,850.266
03.- Crude oil	21,823,912.641	26.- Non-steel metals	4,745,686.194
04.- Minerals	5,743,792.191	27.- Other metals	12,796,681.329
05.- Dairy products	10,236,995.932	28.- Non-electric machinery	16,237,201.183
06.- Fish conservation	1,092,942.403	29.- Electric machinery and equipment	7,088,913.535
07.- Flour and fish oil	3,274,895.027	30.- Transport material	5,397,699.621
08.- Mill products	28,395,158.096	31.- Other manufacturing products	6,310,788.308
09.- Sugar	17,670,672.963	32.- Electricity and water	24,902,386.323
10.- Other foodstuffs	188,856,595.679	33.- Construction	2,856,781.300
11.- Beverages and Tobacco	195,121,295.136	34.- Commercialization services	197,743,005.783
12.- Textiles	13,472,334.231	35.- Transp. & Communication Services	112,406,579.906
13.- Garment industry	7,983,039.795	36.- Financial Services	19,555,484.508
14.- Leather	502,874.516	37.- Insurance Services	3,182,529.387
15.- Shoemaking	346,251.789	38.- Housing/letting services	0.000
16.- Furniture	2,136,000.358	39.- Business services	180,486,368.631
17.- Paper	15,540,458.144	40.- Restaurants & Hotels	1,559,589,852.052
18.- Printing	7,255,186.748	41.- Household commercial services	5,800,919.757
19.- Basic chemicals and fertilisers	26,395,123.453	42.- Household non-commercial services	0.000
20.- Pharmaceuticals	1,525,946.781	43.- Private health services	0.000
21.- Other chemical products	12,478,194.019	44.- Private education services	2,518,707.697
22.- Refined oil	39,304,196.382	45.- Government services	0.000
23.- Plastic	15,678,536.416		

Source: CRG and MEF (2013)

Financial Sustainability: Economic and Social Rates of Return

14. The social rate of return (SRR) is positive under both moderate (Table A6.2) and conservative (Table A6.4) scenarios. The SRR was calculated taking into account both benefits and costs stemming from the Project.²⁰ On the one hand, the benefits of the Project chiefly included the improved quality of tourism services in the region. On the other hand, costs were calculated using a correction factor (CF) of 0.85 that corresponds to the general sales tax (IGV). The CF was applied to investment, operation and maintenance costs.

²⁰Determining the SRR implies the inclusion of a series of social costs and benefits of the Project. Shadow prices are determined on the basis of relative scarcity and social benefits, positive and negative externalities of the Project are included and opportunity costs are taken into account.

Table A6.2. Net Benefits: Moderate Scenario

Year	Incremental Benefits	Incremental Costs	Net Benefits
2014		81,723,359.32	-81,723,359.32
2015		73,257,358.32	-73,257,358.32
2016		59,698,417.26	-59,698,417.26
2017	64,524,503.50	37,535,437.77	26,989,065.73
2018	67,443,408.73	14,999,285.84	52,444,122.89
2019	70,581,099.61	4,570,267.20	66,010,832.41
2020	73,953,977.94	3,901,746.19	70,052,231.76
2021	142,297,553.11	19,434,912.96	122,862,640.16
2022	150,954,369.31	3,722,729.48	147,231,639.84
2023	160,356,762.08	2,428,404.45	157,928,357.63
2024	170,463,875.54	10,072,581.85	160,391,293.69
2025	181,762,742.36	-10,090,839.91	191,853,582.27
2026	193,940,874.14	-10,515,119.15	204,455,993.29
2027	297,656,034.68	-11,686,883.66	309,342,918.33

Discount Rate	9.0%
NPV	626,570,103.37
FRR	28.2%

Source: CRG and MEF (2013)

15. The value-added of the entire program as presented by the Government, which includes tourism and competitiveness, solid waste management and disaster risk management components, is that it multiplies several times the social returns. Without the tourism and competitiveness components, the Net Present Value (NPV) would be around 319 million *nuevos soles* (US\$114 million), while the entire program would approach 530 million *nuevos soles* (US\$190 million). The program yields social benefits that are 60 percent more than without the tourism and competitiveness components (Table A6.3).

Table A6.3. Moderate Scenario's Social Returns: Entire and Partial Programs

Indicator	Entire Program	Program excluding tourism and competitiveness components
NPV	529,373,515.88	319,310,389.27
SRR (%)	28.1%	21.1%

Source: CRG and MEF (2013)

16. The conservative scenario takes into account a lower demand for the product and therefore, a lower number of tourists and spending. However, NPV under those assumptions continues to be positive (Table A6.4). The SRR stands at 22.1 percent, lower than in the moderate scenario, but still higher than the discount rate of 9 percent. In addition, under a conservative scenario, the value-added of the entire program yields 65 percent greater social benefits than a program excluding the tourism and competitiveness components (Table A6.5).

Table A6.4. Net Benefits: Conservative Scenario

Year	Incremental Benefits	Incremental Costs	Net Benefits
2014		69,257,084.17	-69,257,084.17
2015		62,082,507.05	-62,082,507.05
2016		50,591,879.03	-50,591,879.03
2017	37,565,830.50	31,809,693.03	5,756,137.47
2018	38,777,687.30	10,558,368.58	28,219,318.72
2019	40,080,436.66	3,873,107.80	36,207,328.86
2020	41,480,896.84	3,306,564.57	38,174,332.27
2021	92,347,490.82	16,470,265.22	75,877,225.61
2022	97,664,565.70	3,154,855.49	94,509,710.21
2023	103,380,223.42	2,057,969.87	101,322,253.55
2024	109,524,347.90	8,536,086.32	100,988,261.59
2025	116,497,033.40	-8,551,559.25	125,048,592.65
2026	124,019,866.24	-8,911,117.93	132,930,984.17
2027	238,816,188.04	-9,904,138.69	248,720,326.73

Discount Rate	9.0%
NPV	364,464,257.80
FRR	22.1%

Source: CRG and MEF (2013)

Table A6.5. Conservative Scenario's Social Returns: Entire and Partial Programs

Indicator	Entire Program	Program excluding tourism and competitiveness components
NPV	364,464,257.80	236,599,391.76
SRR (%)	22.1%	15.1%

Source: CRG and MEF (2013)

Sensitivity Analysis

17. A sensitivity analysis was carried out using a method that takes into account variations in the cost of investments and yielded solid results for the Project. Variations in the costs of the investment will neither affect the SRR nor the social net present value (SNPV). In both moderate and conservative scenarios in Tables A6.6 and A6.7, variations in the cost of investment either to raise or lower the costs, yield solid SRRs.

Table A6.6. Sensitivity Analysis: Moderate Scenario (Base)

Variation	Investment Cost (nuevos soles)	Social Net Present Value (nuevos soles)
80.0%	165,344,263	498,773,035
85.0%	175,678,279	506,041,865
90.0%	186,012,295	513,310,694
95.0%	196,346,312	520,579,524
100.0%	206,680,328	527,848,354
105.0%	217,014,345	535,117,184
110.0%	227,348,361	542,386,013
115.0%	237,682,378	549,654,843
120.0%	248,016,394	556,923,673

Source: CRG and MEF (2013)

Table A6.7. Sensitivity Analysis: Conservative Scenario

Variation	Investment Cost (nuevos soles)	Social Net Present Value (nuevos soles)
80.0%	165,344,263	335,388,939
85.0%	175,678,279	342,657,768
90.0%	186,012,295	349,926,598
95.0%	196,346,312	357,195,428
100.0%	206,680,328	364,464,258
105.0%	217,014,345	371,733,088
110.0%	227,348,361	379,001,917
115.0%	237,682,378	386,270,747
120.0%	248,016,394	393,539,577

Source: CRG and MEF (2013)

Public finance sustainability

18. The Project's aims at contributing to the development of the Cusco Region, thus the ability of the CRG to meet its financial commitments, is of the outmost importance. The public finance and fiscal aspects discussed below are being revised to accommodate new developments and data.

19. Based on the financial information from the CRG and the operational information and budget execution as of December 31, 2010, the CRG shows a growing trend in its income. A drastic change took place during 2009 following the implementation of the new Government Accounting Plan (*Plan Contable Gubernamental*). During 2009, S/.921.0 million (US\$329 million) were reported as income, while in the previous year, under the old accounting system, the total income was S/.527.8 million (US\$189 million). In 2010, S/.993.4 million (US\$355 million) were reported as income, which represents a 7.9 percent growth in relation to 2009. 97.9 percent of the total income (an average 96.6 percent in the three previous years) corresponds to transfers from the Central Government labeled as ordinary resources aimed at covering current expenses and certain resources originated by their geographic allocation. These funds are characterized by high stability, as shown in the budget execution reports.

20. The income is allocated to administrative expenses (8.2 percent of total collected income in 2010), human resources expenses and social security (66.8 percent) and transfers made to other executing units or special projects for operational expenses and investment plans (21.3 percent). There is also additional income generated in previous periods and pending collection, which accounts for less than 10 percent of the total income but presents an increasing opportunity for income generation.

21. The CRG did not need to borrow funds from national or foreign financial institutions, except from funds corresponding to internal debt originated by the Emergency Decree N° 040-2009, meant to fund public investment projects, but it does not generate financial expenditures. After expenditures were allocated for current needs and investments as well as for the payment of other commitments, the CRG had a net surplus of S/.76.7 million (US\$27.4) in 2010, and despite being 50.8 percent of the surplus from 2009 (S/.155.7 million, US\$55.7), it shows the institution's capacity to generate resources and accumulate them for future periods.

22. The total liabilities of the CRG have increased by 5 percent from 2009 to 2010, rising from 450 million nuevos soles (US\$161 million) in 2009 to 470 million nuevos soles (US\$168 million) by December 2010. This noticeable increment is due to higher provisions for social benefits, which grew from 283 million nuevos soles (US\$101 million) in 2009 to 366 million nuevos soles (US\$131 million) in 2010. Nonetheless, there is a decrease of S/.60 million (US\$21 million) in current liabilities, mainly due to the lower amount of accounts payable, which reached S/.7.7 million (US\$2.8 million), from S/.51 million (US\$18 million) in 2009.

23. The debt stock, as measured by fiscal rules, does not consider provisions for workers' social benefits. Thus, the debt stock amounts to S/.107 million (US\$38 million), from less than S/.52 million (US\$18.6 million) in 2009, and the short term debt is S/.39million (US\$14 million), from S/.60 million (US\$21 million) in 2009. Based on the debt stock, the liabilities of the CRG are low, representing a debt ratio of 0.40 in relation to the total equity, and are mainly due to accounts payable for goods and services suppliers, provisions for social benefits payments and contingencies that might result from court rulings related to labor issues.

24. On the other side, liquidity ratios are quite good: 2.94 by December 2010, and 1.45 in 2009, explained not only by the low debt level of the CRG, but also by its high capacity for cash flow generation.

25. Regarding the regulatory framework for indebtedness of Regional and Local Governments defined by the Law of Prudence and Transparency – Law N° 27958 (which modifies law N° 27245), the CRG does not comply with a rule on primary result. The Law requires that the average of the last three years' primary results be positive. However, the non-compliance with this requirement does not imply inability to pay. Other variables generate this result, such as the ability to invest or spend in a timely manner; nevertheless, this situation does not affect cash or available resources, and the balance was S/.181 million (US\$64.8 million) by the end of 2010.

26. Based on the financial information review and considering other social and institutional factors, the Committee of Assessment of *Class & Asociados* S.A. Risk Rating Agency assigned a BBB- risk rating for the long term debt. This rating is assigned to institutions or financial instruments that present adequate capacity to meet its financial commitments, both capital and interests, in the agreed conditions and timeline. However, adverse economic conditions or changing circumstances might weaken the obligors' capacity to meet its financial commitments.

27. *Financial and Economic Analysis of the solid waste component.* The solid waste management infrastructure will be designed to be least cost, considering political, technical, social and environmental limitations evaluated, as part of the feasibility study and accompanying environmental study. For the solid waste component, in order to determine the feasibility of applying the *fideicomiso*, it was necessary to review the income and current and capital expenditures of each Province and municipal District. This analysis indicates that most of the municipalities can cover operating and maintenance costs estimated for the future in pre-investment studies, using intergovernmental transfers and tariffs. However, in the event any municipality could not cover all operation and maintenance costs, the Bank is exploring options with the CRG in order to cover the deficit of resources for these special cases so municipalities are not left without a solution to the problem of collection and solid waste disposal.