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PROJECT APPRAISAL DOCUMENT  
ON A  
PROPOSED CREDIT  
IN THE AMOUNT OF SDR 6.2 MILLION  
(US\$8.0 MILLION EQUIVALENT)  
TO THE  
REPUBLIC OF HONDURAS  
FOR AN  
ACCESS TO LAND PILOT PROJECT (PACTA)

November 3, 2000

Environmentally and Socially Sustainable Development Sector Management Unit  
Central America Country Management Unit  
Latin America and the Caribbean Region Office

## CURRENCY EQUIVALENTS

(Exchange Rate Effective November 1, 2000)

Currency Unit = Honduran Lempira  
Lps. 14.92 = US\$1  
US\$0.067 = 1 Honduran Lempiras

## FISCAL YEAR

January 1 December 31

## ABBREVIATIONS AND ACRONYMS

CMAT	Land Administration Component Modernization, PAAR Project (see below)
FAO	Food and Agriculture Organisation of the United Nations
FI	Private Financial Institution
FONADERS	Fondo Nacional de Desarrollo Rural Sostenible (National Fund for Sustainable Rural Development)
FUNDER	Fundación de Desarrollo Rural de Honduras (Rural Development Foundation of Honduras)
HIPC	Highly Indebted Poor Countries Initiative
INA	Instituto Nacional Agraria (National Agrarian Institute)
I-PRSP	Interim Poverty Reduction Strategy Program
LMDSA	Ley de Modernización y Desarrollo del Sector Agrícola (Agricultural Sector Modernization and Development Law)
NGO	Non-governmental Organization
OPD	Organización Privada de Desarrollo (Private Development Organization)
PAAR	Proyecto de Administración de Areas Rurales (Rural Land Management Project)
PACTA	Programa de Acceso a la Tierra (Land Access Pilot Program)
PILARH	Proyecto de Iniciativas Locales para el Autodesarrollo Regional de Honduras (Local Projects and Initiatives for Regional Self-Development)
PRODELCA	Programa de Desarrollo Local y Cambio Social (Program of Local Development and Social Change)
PROLANCHO	Proyecto de Desarrollo Rural Olancho (Olancho Rural Development Project)
PROLESUR	Programa de Lempira Sur (Lempira Sur Rural Development Program)
PRONADERS	Programa Nacional de Desarrollo Rural Sostenible (National Program of Sustainable Rural Development)
PRSP	Poverty Reduction Strategy Program
SAG	Secretaria de Agricultura y Ganaderia (Secretariat of Agriculture and Livestock)
SyEP	Seguimiento y Evaluacion Participativa (Participatory Monitoring and Evaluation)
UTA	Unidad de Gestion (Technical Administrative Unit)
UTL	Unidad Tecnica Local (Local Technical Unit)
UNDP	United Nations Development Programme

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Sector Director:	John Redwood
Task Manager:	Augusta Molnar

**HONDURAS**  
**ACCESS TO LAND PILOT PROJECT (PACTA)**

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IBRD 31203

**HONDURAS**  
Access to Land Pilot Project (PACTA)

**Project Appraisal Document**

Latin America and the Caribbean Region  
Central America Country Management Unit

<p><b>Date:</b> November 3, 2000</p> <p><b>Country Manager/Director:</b> Donna Dowsett-Coirolo</p> <p><b>Project ID:</b> P055991</p> <p><b>Lending Instrument:</b> Specific Investment Loan (SIL)</p>	<p><b>Team Leader:</b> Augusta Molnar</p> <p><b>Sector Manager/Director:</b> John Redwood</p> <p><b>Sector (s):</b> AY – Other Agriculture</p> <p><b>Theme (s):</b></p> <p><b>Poverty Targeted Intervention:</b> Y</p>																														
<p><b>Project Financing Data</b></p> <p><input type="checkbox"/> Loan    <input checked="" type="checkbox"/> Credit    <input type="checkbox"/> Grant    <input type="checkbox"/> Other (Specify)</p> <p><b>For Loans/Credits/Others:</b> <b>Amount (US\$m):</b> 8 million (SDR 6.2 million)</p> <p><b>Proposed Terms:</b> Standard Credit</p> <p><b>Grace period (years):</b> 10</p> <p><b>Commitment fee:</b> Standard: a variable rate between 0 and 0.50% of the undisbursed credit balance set annually by the Executive Directors of IDA.</p> <p style="text-align: right;"><b>Years to maturity:</b> 40</p> <p style="text-align: right;"><b>Service charge:</b> 0.75%</p>																															
<table border="1" style="width: 100%; border-collapse: collapse;"> <thead> <tr> <th style="text-align: left;">Financing Plan:</th> <th style="text-align: left;">Source</th> <th style="text-align: right;">Local</th> <th style="text-align: right;">Foreign</th> <th style="text-align: right;">Total</th> </tr> </thead> <tbody> <tr> <td>IDA</td> <td></td> <td style="text-align: right;">7.22</td> <td style="text-align: right;">0.78</td> <td style="text-align: right;">8.00</td> </tr> <tr> <td>FINANCIAL INTERMEDIARIES</td> <td></td> <td style="text-align: right;">6.84</td> <td style="text-align: right;">0.00</td> <td style="text-align: right;">6.84</td> </tr> <tr> <td>GOVERNMENT</td> <td></td> <td style="text-align: right;">0.60</td> <td style="text-align: right;">0.00</td> <td style="text-align: right;">0.60</td> </tr> <tr> <td>BENEFICIARY GROUPS</td> <td></td> <td style="text-align: right;">1.55</td> <td style="text-align: right;">0.00</td> <td style="text-align: right;">1.55</td> </tr> <tr> <td><b>Total:</b></td> <td></td> <td style="text-align: right;">15.97</td> <td style="text-align: right;">1.03</td> <td style="text-align: right;">17.00</td> </tr> </tbody> </table>		Financing Plan:	Source	Local	Foreign	Total	IDA		7.22	0.78	8.00	FINANCIAL INTERMEDIARIES		6.84	0.00	6.84	GOVERNMENT		0.60	0.00	0.60	BENEFICIARY GROUPS		1.55	0.00	1.55	<b>Total:</b>		15.97	1.03	17.00
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<p><b>Borrower:</b> REPUBLIC OF HONDURAS</p> <p><b>Responsible agency:</b> NATIONAL AGRARIAN INSTITUTE, THROUGH ADVISORY BOARD OF PACTA</p> <p>National Agrarian Institute (INA), Ministry of Agriculture and Livestock Address: Tegucigalpa, Honduras Contact Person: Abgo. Anibal Delgado Fiallos, Minister Tel: 504 232-4893      Fax: (504) 232-4893      Email: janibal@hondutel.hn</p> <p>Other Agency(ies): Project Coordination Unit (PAAR), Ministry of Agriculture and Livestock Address: Edificio Florencia, Boulevard Suyapa, Tegucigalpa, Honduras Contact Person: Ing. Ricardo Arias Tel: 504 239-4411      Fax: 504 239-0549      Email: paar@hondudata.com</p>																															
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<p><b>Project implementation period:</b> 3.5 years</p> <p><b>Expected effectiveness date:</b> 03/31/2001    <b>Expected closing date:</b> 12/31/2004</p>																															

## **A. Project Development Objective**

### **1. Project development objective:** (see Annex 1)

The objective of Land Access Pilot Project (PACTA) is to support the acquisition of land and the formation of sustainable farm enterprises by self-organized landless and land-poor peasant families. The pilot will test a public/private partnership strategy, with the private sector lending for land purchase and the use of public sector funds, through the project, supporting complementary investments, and technical assistance to improve the productivity of the newly acquired properties. If successful, the Government would consider scaling up the pilot to a national program in several years.

### **2. Key performance indicators:** (see Annex 1)

#### Performance Indicators (Impacts)

1. About 1600 farm families participate in local land markets and establish sustainable farm enterprises;
2. Private financial institutions increase lending for land purchase by groups of small farmers;
3. Beneficiary incomes increased through improved land productivity and output in project sites; and
4. Decentralized model for land access tested.

#### Performance Indicators (Outputs)

1. Number of sub-project proposals prepared and loans approved by private lenders;
2. Number and area of properties acquired and farm enterprises established;
3. Number of families who participate in the enterprises; and
4. Loan repayment performance by beneficiaries.

## **B. Strategic Context**

### **1. Sector-related Country Assistance Strategy (CAS) goal supported by the project:** (see Annex 1) **Document number:** 20072-HO      **Date of latest CAS discussion:** December 14, 1999

The CAS overall goal is to support Honduras' reconstruction and transformation after Hurricane Mitch, with a strong emphasis on social equity. One specific goal within this context is the promotion of sustainable rural development. The CAS identifies a need for improved land tenure security and access to credit and land markets as key elements of sustainable rural development. In preparation for Honduras' entry into the HIPC Initiative, an I-PRSP was prepared and reviewed, and work is advancing on the elaboration of a full PRSP. Among the rural sector issues which are raised in the CAS and will need to be addressed in the PRSP are: the lack of access to land and problems of land security; inadequate rural finance, especially for smallholders; and the need for effective systems of agricultural and rural technical extension. One of the key actions to address some of these issues is the creation of a fund to support financing of land purchases, supported by complementary investments to increase productivity and sustain productive enterprises, with technical assistance from NGO and other private providers. This effort complements on-going activities financed under the Rural Land Management Project (PAAR, Cr. 2940-HO) to modernize the land administration system (cadastre, registry, and land titling system).

### **2. Main sector issues and Government strategy:**

Land reform and land titling have been major policy objectives in Honduras for the last several decades. Over this period, more than US \$40 million was invested in cadastre, about 125,000 titles were issued by the National Agrarian Institute (INA), and attempts were made to transfer significant areas of underutilized private and public land with agricultural potential to *minifundistas* and rural landless families. Nonetheless, Honduras continues to have a large, poor rural population and a highly skewed land

distribution. Much of the land distributed to land reform cooperatives formed for this purpose was not legally transferred, and most reform cooperatives have disbanded or lost the majority of their membership. Currently, 70 percent of landholdings (numbering about 225,000 with less than 5 ha. as of 1993) account for about 10 percent of land in farms; and a little over 1 percent of farmers (around 3,500) own about 25 percent of the land. The landless rural population (excluding workers regularly employed in the agro-export sector) and *minifundistas* together account for about 50 percent of the rural population. Most landholders with less than 5 hectares are not titled, nor are most of them eligible for titling because they work rented or borrowed land under informal, short-term arrangements, or because they occupy plots within public forest lands ineligible for titling. The structure of rural landholding in Honduras, as indicated by the most recent census data (1993), reflects at least three long-term trends: i) increased occupation of forest land, especially in Olancho and Colón; ii) the increasing formation of *minifundios* (plots less than 1 ha); and iii) a sharp reduction in the number of producers still organized in cooperatives (originally 3,500). This is despite the fact there are numerous examples of small scale farms functioning as highly profitable enterprises assisted by grass-roots NGO programs.

In the 1990s, Government initiated a comprehensive reform of the rural sector, recognizing the failure of earlier efforts to effect significant land redistribution or to fuel growth. A policy framework was embodied in the Agricultural Sector Modernization and Development Law (1992) which aimed to: (i) eliminate subsidies and credit, price, and tariff distortions; (ii) focus the mandates of the National Agrarian Institute (INA) more narrowly on titling of public lands to producers (mainly those already settled on those lands); (iii) recognize public, private, and municipal rights to forests, thereby creating incentives for sound resource management; (iv) create a land fund mechanism for land purchase; and (vi) increase access to rural credit. Not all mandates have been successfully implemented. In recent years, the country has undertaken serious efforts to modernize the land administration system, both legal and physical land records, target the land titling program to the large number of settlers in frontier areas; and title indigenous communities and recognize parts of ancestral domains. However, a program to increase access to land is still needed.

Access to rural finance has also remained very limited, and Government efforts to reform the state agricultural development bank have had little impact in expanding credit services to small-scale farmers and rural entrepreneurs. Numerous communal revolving credit groups have been established in recent years, but they are fragile institutions with little capacity to weather cyclical downturns and no linkage with the formal financial system. The effects of Hurricane Mitch in 1998-99 have further depressed credit markets, as many of those producers who have obtained access defaulted on crop or agribusiness loans, affecting the liquidity of private sector financial institutions.

### **3. Sector issues to be addressed by the project and strategic choices:**

Recognizing that the impacts of Hurricane Mitch were partly related to the unsustainability of natural resources management, the concentration of development resources on low-lying areas, and the inability to provide productive alternatives for the land-based rural poor, the Government's post-Mitch rural strategy has three broad principles: improved targeting of the rural poor, strengthening of decentralized institutions, and sustainable watershed management. In the rural sector, the Government has prioritized access to land and credit as key to promoting economic growth with poverty reduction, to be achieved by: (i) land titling and registration to improve land security and the functioning of land markets; (ii) piloting a market-assisted land access program to reduce the skewedness of land distribution; (iii) and increasing access to rural finance.

In preparing an operational strategy to expand access to land and credit, the government of Honduras is

able to build on several assets. First, INA's own long experience in land reform and titling has provided important expertise on rural ownership and land-use and successful mechanisms of conflict resolution. Second, the land administration modernization program (CMAT) is providing a secure basis for land titling and functioning of land markets, both in the pilot area of Comayagua and areas with complementary donor activities. Third, Honduras has a long tradition of private farmer-to-farmer research and extension services geared to low-investment technologies proven in upland settings, which ensures availability of small farm technologies on diverse land types and which provides a network of qualified NGOs and small firms as service providers. Fourth, some private financial institutions have experimented with land purchase schemes. Fifth, there are active area-based rural development initiatives being coordinated by NGOs or project units in regions where there is a clear demand for and availability of private land for purchase. Sixth, there is considerable research data regarding subsistence, mixed and commercial land-based enterprises in lands of different aptitudes, from which to develop sound financial projections for credit operations.

With the broadening of strategic discussions after Hurricane Mitch, INA has engaged a variety of stakeholders in a dialogue about design options for a land fund pilot. Despite concern by some of the peasant organizations that the land reform agenda is not complete, there is broad agreement that improving access to land markets requires the long-term participation of private sector financial institutions and that a pilot needs to test potential models of achieving this. Given the innovation of the PACTA model, government has also decided to initiate this as a small pilot operation, studying carefully the results before launching the program on a national scale. Civil society would be actively involved in participatory monitoring and evaluation.

### C. Project Description Summary

1. Project components (see Annex 2 for a detailed description and Annex 3 for a detailed cost breakdown):

Component	Sector	Indicative Costs (US\$M)	% of Total	Bank-financing (US\$M)	% of Bank-financing
Technical and Legal Assistance to Rural Producers, includes consultant services for pre- and post-land purchase activities by local technical assistance units (UTLs--those eligible NGOs and rural area development project coordination units identified in the program area). TA includes legal assistance, promotion /communication, business proposal preparation, land market information, skills in organization, and farm extension.	Other Agriculture	1.17	6.9	1.17	14.6
Land Purchases by producer groups, includes financing provided by private financial institutions for acquisition of land, fixed assets and working capital.	Agricultural Credit	6.84	40.2	0.00	0.0
Complementary Subprojects, includes support for formation of viable enterprises by means of grants for complementary investments. Grants would be limited to 45 percent of the value of the overall farm business plan.	Other Agriculture	7.16	42.1	5.60	70.0
Project Administration includes management of the PACTA pilot by a coordination team recruited and supervised by FAO, as well as support by an advisory board, feasibility studies, monitoring and evaluation, financial management and reporting and quality control.	Other Agriculture	1.83	10.8	1.23	15.4
<b>Total Project Costs</b>		17.00	100.0	8.00	100.0
<b>Total Financing Required</b>		17.00	100.0	8.00	100.0

## **2. Key policy and institutional reforms supported by the project:**

The project opens an alternative path for increased access to agricultural land by the rural poor, that is consistent with the fundamental government goal of improving support for land tenure security. No specific institutional or policy reforms are required for project implementation. A Presidential Decree has been passed (No.893-00; June 27, 2000) which establishes the Program for Land Access (PACTA) under the general policy mandate of the National Agrarian Institute (INA) to provide technical support and complementary financing to producer groups purchasing land for productive, land-based investments.

## **3. Benefits and target population:**

**Target population.** The basic criteria for eligibility to participate in the project are derived from existing law, in particular the Agricultural Sector Modernization and Development Law of 1992. These criteria establish the target population as landless and land-poor (< 5 ha) families whose primary occupation is agriculture. Since these criteria would include such a large part of the rural population, the local technical units (UTL) contracted to implement the program would have the flexibility to apply priorities in their respective areas that would also be compatible with the decision-making criteria of the participating private financial institutions. In general, priority would be given to peasant producers with scarce economic resources and precarious or no access to land, and to those with prior experience working as a group (though not necessarily for production activities).

**Benefits.** The pilot program is intended to obtain the following benefits:

1. Sustainable increase in the income and capacities of approximately 1,600 families selected from within the target population.
2. Increased productivity and adoption of sustainable production practices on land acquired through the program.
3. Increased participation of private financial institutions in serving small scale producers and adopting an appropriate methodology for addressing the needs of such clients.
4. Pilot testing of the program for eventual expansion on a national scale.
5. Strengthening of local capacity by training participating UTLs in appropriate methodologies for identifying economically viable sub-projects, preparing appropriate business plans, and providing technical assistance for their execution.

## **4. Institutional and implementation arrangements:**

The National Agrarian Institute has been designated by the Honduran government to take the lead role in launching PACTA. Under Decree 893-00, the Minister-Director of INA chairs a Board of Directors which is an advisory council for PACTA, with membership from the Vice-minister of Agriculture, two representative private financial institutions, two UTLs, three representatives of peasant organizations, including one representative of the Federation of Peasant Women (Confederación de Mujeres Campesinas de Honduras). This advisory Board will supervise the implementation of PACTA by an administrative unit (UTA), under the administration of INA but physically located within FAO. This arrangement is intended to provide operational independence to the UTA and, in turn, to the local institutions contracted to provide services to participants. Other advantages, especially important in the pilot phase of the Program, include the fact that:

- The UTA would benefit from established FAO practices in managing program funds and financial reporting, compatible with World Bank requirements;
- PACTA could be launched with less administrative complexity than is common to many projects in

Honduras, thus enabling the focus to be placed on technical issues and getting the program to work in the field;

- The local representation of FAO has a long-term experience in rural land policy and natural resource management in Honduras and would thus bring considerable 'value-added' to the project.

At the regional field level producer families will be identified and provided technical assistance by UTLs (local NGOs and other entities with the required experience, as specified in the Operational Manual of PACTA). These UTLs will be remunerated on a per family basis by the UTA for services provided pre-and post-land purchase. Eligible UTLs can include NGOs, projects, programs, or community organizations, and other private service providers. Prior to contracting any UTL, the UTA would evaluate eligibility including ability to provide continuity of services. A number of UTLs have been prequalified for the pilot phase: (i) PROLANCHO, an EU assisted project, (ii) PROLESUR in Lempira Sur, an FAO-assisted project, (iii) PRODELICAS (which operates under the Diocese of Trujillo); and three NGOs -- (iv) FUNDER, (v) PILARH, (vi) Fundacion FINACOOOP. The UTLs that the project preparation team identified all have a proven record of success in developing sustainable programs in rural development. One, PILARH, is an independently operating NGO with a 15-year track record, whose program includes land purchase and enterprise formation for landless peasants in Copán and Lempira. All UTLs have credit programs and some have made initial attempts to facilitate land purchase. All embrace a highly participatory model in the implementation of their respective programs. One motive for selecting this model, apart from the desire to avoid a heavy central administration, is to build up local technical capacity in each UTL to incorporate PACTA into the framework of other, local initiatives related to land management, credit, and technical services. [See Annex 11, Social Evaluation]

Initially, each UTL would work in a single region roughly coinciding with the boundaries of different departments. Some UTLs have the capacity to expand operations into more than one area. The regions to be included in the pilot are among the poorest in the country: Copán, Lempira, Colón and Olancho. An additional region, Comayagua, is where the IDA-supported land administration project is underway.

The UTL will be hired on a fee-for-service basis, at a maximum cost (\$225) per family applicable to the entire process of sub-project preparation up to and including the presentation of a proposal to one of the participating financial institutions. As an incentive, 50% of this cost would be held back pending approval of the proposal by a financial institution. The cost parameters agreed upon with the UTLs are in line with those of the Upland Fund supported under IDA Credit 2940-HO, and also coincide with established costs of PILARH, which has been performing very similar work, albeit on a small scale. Follow-up technical assistance, post-loan approval, would be based on a contractual arrangement with the participants; these costs would be reimbursed up to a maximum of \$230 per year per family. During this phase, the newly formed enterprises would decide either to continue to use the UTL or to hire any other approved private service provider. The project would require participants to partially defray the cost of these services starting in the second year. The land purchase-sale agreement itself will be privately negotiated between the prospective buyers and landowners.

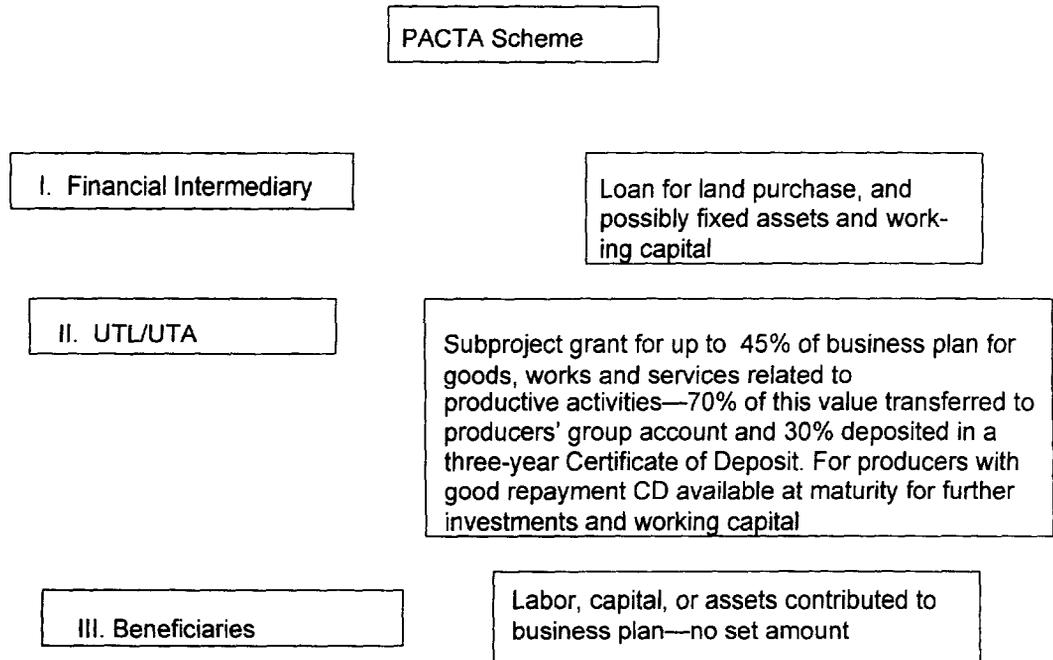
#### Loan and Grant Financing Mechanisms

Business plans will be prepared for each farmers group which is negotiating purchase of a property. The plans will include a component for land purchase (and possibly productive investments to be financed mainly by a financial institution), a second component for complementary investments and working capital (to be financed mainly through the project on a grant basis) and contributions from beneficiaries (in cash and/or in kind). Once a business plan is submitted to a participating Financial Institution (FI) by a producer group (assisted by the UTL), the FI will evaluate the proposal and make its own decision about

whether to provide a loan for the land purchase component and, in selected cases, for other investments and working capital. The component for eligible goods, works and services (to be financed by a grant with the Credit proceeds) should not exceed 45% of the total business plan cost, or US\$ 3,500 equivalent per family, whichever is smaller. In addition, the business plan will include expected beneficiary contributions in the form of labor, capital, and/or assets. The UTA will review the business plan for consistency with project guidelines, and will approve the grant for complementary investments and working capital once it has been notified of preliminary approval of the land loan by the FI.

Seventy per cent (70%) of the subproject grant will be transferred by the UTA to an account set up for the producers, to finance business plan improvements and working capital needs during the first several years of the enterprise establishment. The remaining 30% will be deposited in a Certificate of Deposit (CD) with a three-year maturity to be used by the group for further complementary investments and working capital to continue improving the productivity of the properties.

Annual reviews of project performance will assess the performance of producer groups with particular attention to the financial viability of the farms, and with a view to refining the loan and grant financing arrangements as necessary.



Technical Assistance Provision by the UTLs

The UTLs are expected to integrate PACTA into the framework of other established programs, focusing at least initially on the groups and communities whom they presently work. This strategy will enable PACTA

to be incorporated in a coherent fashion in the context of other more comprehensive rural development initiatives (e.g., related to land management; soil and water conservation; technology transfer; credit; marketing; women's participation) instead of being treated as an isolated program. This has an additional benefit in terms of project costs: the payment for services was negotiated on the basis of the marginal costs associated with adoption of the program in an existing operation, thus keeping overhead low. In addition, the UTLs will perceive non-monetary benefits in being able to facilitate access to the program for their client base, developing new tools for follow-up and evaluation, and training. The UTLs will be reimbursed according to a fixed cost per family calculation as part of a consultant services contract with the UTA. The contract will be annual and based on the number of families being served at a given time.

The UTLs are expected to establish relations with a local support committee (Comité Local de Apoyo; CLA). The CLA would be any locally established representative group in civil society that may facilitate the process of identifying candidates to participate in PACTA and that may also help to transmit information about PACTA.

Given the likely level of demand for participation, the UTLs are not expected to conduct broad based publicity campaigns during the pilot phase, but will instead make information about PACTA available mainly through the normal operations of the UTLs.

Prior to concluding any contract with a UTL, the UTA will publish terms of reference and assess the agency's qualifications and experience, on the basis of criteria established in the project Operating Manual. A legal evaluation has been conducted (available in the project files) and has shown that the prospective UTLs are clearly qualified to enter into the type of contracts planned for PACTA.

Given the arrangements being tested in the pilot phase, and in particular the decentralization of field operations in different regions to different local agencies, a strong commitment to a program of participatory evaluation has been included in the design. This aspect of the project, which will be coordinated by the UTA, would facilitate a regular process of information exchange, identification of program weaknesses, and adjustments as needed during the pilot phase.

## **D. Project Rationale**

### **1. Project alternatives considered and reasons for rejection:**

The following alternatives were considered and rejected:

- (a) Establish a government sponsored trust fund for financing land purchase--this would not have sustainability over time given Honduras' tight fiscal position, nor would it encourage longer-term investment financing by the private sector for land acquisition by smallholders and rural poor;
- (b) Centralize decision-making for selection of beneficiaries for land purchase and complementary subprojects in a "land fund agency"--it was decided that it was more cost-effective and in line with the government's decentralization policies to rely on existing rural development technical assistance units in the country with good knowledge of the potential beneficiaries, thereby reducing administrative costs of the initiative;
- (c) Encourage a more effective rental market rather than promoting land purchases--while seasonal rental arrangements are important in Honduras, there are few long-term leases, and rental markets would not create the same opportunities for capable rural producers to gain access to land, nor would there be incentives for environmentally sound investments in soil and moisture conservation; and
- (d) Disburse the full amount of the grant for complementary investments and working capital to the

producers for the productive subprojects at the time of loan approval, rather than delaying release of part of the resources to the third year. This was rejected, partly to create an incentive for timely repayment of the private loans and to provide additional investment and working capital at a time in the development of the farm enterprise when groups are already well established and capable of further improvements. (See Annex 4 for a model of financial flows and farm returns).

**2. Major related projects financed by the Bank and/or other development agencies (completed, ongoing and planned).**

Sector Issue	Project	Latest Supervision (PSR) Ratings (Bank-financed projects only)	
		Implementation Progress (IP)	Development Objective (DO)
<b>Bank-financed</b> Agriculture and Natural Resources; Land Administration Public Sector Modernization  Biodiversity Conservation  Disaster Prevention	Rural Land Management Project (Cr. 2940-HO)	S	HS
	Public Sector Modernization TAC (Cr. 2814; US\$9.6 million);	S	S
	Public Sector Modernization SAC (Cr.28160-3; US\$101.50 million)		
	Biodiversity in Priority Areas Project (GE-44343)	S	S
	Natural Disaster Mitigation (Cr. R/2000-73)	S	S
<b>Other development agencies</b>			
FAO	Rural Development Project Lempira Sur		
European Union	PROLANCHO (Rural Development)		
European Union	Land Program and Support for Food Security in Honduras		
Government of Honduras	PRONADERS (National Program of Sustainable Rural Development)		
PILARH (NGO)	XXXX		
IFAD	FONADER--(Natural Fund for Sustainable Development)		
Land Fund and Food Security	Land Program and Support for Food Security in Honduras (European Union)		

IP/DO Ratings: HS (Highly Satisfactory), S (Satisfactory), U (Unsatisfactory), HU (Highly Unsatisfactory)

### **3. Lessons learned and reflected in the project design:**

The Bank has been gaining experience over the years in promoting access to land, and the task team consulted the Land Thematic Group to discuss this experience in the design of PACTA.

- A financial scheme limited to land purchase alone will likely fail or tend to benefit only those individuals with access to significant additional resources. Complementary financing for improvements and working capital, along with technical assistance, are essential for projects intended to benefit the rural poor.
- Grants to co-finance new farm enterprises should be used in a clear and limited fashion. Financial intermediaries which assume the full credit risk should be able to select the beneficiaries, and approve the business plan.
- An incentive structure should be created that encourages producers to negotiate the lowest possible price of land. In PACTA grants do not apply to land purchase, nor is the interest rate on loans subsidized. A portion of the grant is tied to the repayment record established by the buyers.
- Precautions should be taken where possible to avoid speculative increases in the price of land in anticipation of the program. In PACTA, the pilot phase of the program will be implemented in 5 different regions, thus avoiding a substantial impact on the land market in any one area.
- The program should not impose any particular model of association or production; such decisions rightfully belong to the participants in the program. However, producers with prior experience working as a group are more likely to succeed in establishing a new enterprise.
- The program should not create new decentralized institutional arrangements if it can draw on relevant institutions already in the field. PACTA takes advantage of local capacity for pre-selection of beneficiaries by sub-contracting technical assistance during all phases of the process.
- The program should not be subject to political bias and stakeholders should participate actively in oversight and development of program norms. To these ends, the Board of Directors (Consejo Directivo) of PACTA involves all stakeholders: government holds two of nine positions; financial institutions and UTLs each have two representatives; and producer organizations have three.

### **4. Indications of borrower commitment and ownership:**

The President of Honduras issued an Executive Decree No.893-00 of June 27, 2000 that established PACTA. The program has been declared to be an important component in the Plan Maestro de Reconstrucción y Transformación Nacional (Master Plan for Reconstruction and National Transformation) and the Estrategia Nacional de Reducción de la Pobreza (National Strategy for Poverty Reduction), as reflected in Honduras' I-PRSP.

The government has initiated negotiations with FAO for technical assistance to establish the administrative unit of PACTA, thus demonstrating its vision that government's role, while important, should focus on leadership on policy and normative issues rather than implementation. A detailed draft Operational Manual has been prepared and will be approved by IDA by Credit effectiveness.

INA has presented PACTA to different producer organizations and demand for access to the Program has already been widely expressed.

### **5. Value added of Bank support in this project:**

IDA is supporting the initial phase of land administration reform, cadastre and systematic land adjudication under the ongoing Rural Land Management Project (PAAR, Credit 2940-HO), and has thus accumulated a

good deal of experience in country on land tenure issues.

A great deal of World Bank sponsored research and analysis on the issues related to the efficiency of family farms, the importance of increasing access to land as means of attacking rural poverty, and the broad support for participatory approaches to rural development have enabled this project to be prepared in an atmosphere of constructive dialogue.

Creating access to land and credit markets is a stated aim of the I-PRSP, and the government considers the World Bank's support in implementing a viable model is important.

## **E. Summary Project Analysis** (Detailed assessments are in the project file, see Annex 8)

### **1. Economic (see Annex 4):**

Cost benefit      NPV=US\$ million; ERR = % (see Annex 4)

Cost effectiveness

Other (specify)

Data was collected for six with and without project farm models representing different agro-ecological conditions. Four farm models are from the Pacific slope region and two are from the Atlantic coast region (see Table 1). For each farm model, data was collected on production and recurrent and investment costs. The results show that in all cases the farm models have sufficiently positive net present values at a nine percent discount rate.

### **2. Financial (see Annex 4 and Annex 5):**

NPV=US\$ million; FRR = % (see Annex 4)

The farm models discussed in Annex 4 and documented in the project file (Olinto, 1999 and Barahona, 1999) demonstrate the essential financial viability of the proposal. The models were derived from field work (1999) by FAO in different regions representing a wide variety of conditions. Other data generated in the course of project preparation also confirmed the validity of the models. All of the models are based on analysis of small scale (< 5 ha) producers, drawing on the particular experience of poorer hillside producers. In this sense, the assumptions are very conservative. The results are encouraging because they indicate the feasibility of adopting the program even in the poorest regions and under difficult conditions.

Three private financial institutions have been evaluated during preparation and details are available in the project file. These institutions have the required liquidity and portfolio spread to be able to participate in the project. Other institutions also may wish to participate during the period of implementation; eligibility criteria will be detailed in the project operation manual.

Fiscal Impact:

The fiscal impact of the project is negligible since the grants and technical assistance are mainly financed through the IDA Credit, and land purchase credit will come from private financial intermediaries using their own resources.

### **3. Technical:**

The UTLs selected for the start up of the project all have good ongoing programs in Honduras. However, there are two areas where the UTA will need to facilitate training for some UTLs to assure the full range of services required: (i) legal services; and (ii) commercialization (i.e., marketing). Provision has been made in the project for such capacity building.

The UTLs will be the main providers of technical and legal services to producer groups who wish to develop a proposal for financing. Among these groups, some will require more substantial assistance than others. PILARH works with groups composed of landless peasants with little or no experience in any group endeavor; but the Social Evaluation also detected that there are many groups already established in one form or another, who would be good candidates for participation in PACTA and who would have priority over less organized candidates. The project will facilitate legal, organizational, technical and marketing services to eligible groups.

#### **4. Institutional:**

Project preparation included a detailed assessment of alternative institutional arrangements and the legal framework for these. Institutional analysis was carried out in several steps: in early planning workshops with government officials and sector specialists, as part of the social assessment, in an analysis of financial institutions, in a study to define eligibility criteria for local implementing units (UTLs), in the legal analysis, and in the design of participatory monitoring and evaluation models. It was agreed that GOH should play a promotional and normative role through INA, but not act directly as an implementing agency. It was also agreed that the pilot would work as much as possible through existing institutions. Project files contain all of the above-mentioned assessments.

##### **4.1 Executing agencies:**

**Instituto Nacional Agrario (INA).** This institution is responsible for land administration in Honduras and is the lead entity for the land administration component of the PAAR project (Credit 2940-HO). The Minister-Director of INA has taken a strong lead in promoting PACTA from the earliest stages of preparation of the proposed project. INA will not have a direct operational role, but rather will focus on normative issues and promoting access to land at the policy level.

##### **Local Technical Assistance Agencies (UTLs)**

A legal analysis of the five UTLs expected to participate in the project showed that all operate autonomously, including two that operate with external financing, two non-profit associations, and two foundations. The assessment of these organizations as qualified to provide services in the framework of PACTA does not preclude others from emerging as candidates during the pilot phase.

On an operational level, the UTLs identified during preparation all manage programs entirely compatible with the objectives of PACTA. All have excellent track records and sufficient expert or well trained staff to provide basic services.

Both the UTLs and producer groups formed to participate in PACTA can also use private service providers of technical assistance and training. While it is expected that the UTLs will be responsible for most technical oversight during the pre-loan phase, the role of other private service providers may be greater in the phase following loan approval.

##### **Qualified Lending institutions**

At present, three FIs have qualified to finance loans to producers under the project based on agreed criteria. If additional FIs wish to participate, they would have to agree to an independent assessment of their eligibility using the same criteria. All FIs will need to be certified annually by the National Commission on Banks and Securities. No institution will be allowed to serve as both an UTL and FI in the same geographic region.

**Banco de Occidente.** This institution has the second most extensive network of branches (96 total) in

Honduras. Historically, it has been fairly active in providing financial services to the rural population, including in the period after Mitch. Although credit for agricultural land purchase has been available in Honduras only on an extremely sporadic basis, Banco de Occidente does have some experience in this regard. It has regional managers skilled in analyzing the credit needs and business plans of small producers, 5 of whom participated in a recent RuralInvest course with the UTLs and other financial institutions. The RuralInvest software has been installed in a number of branches of Banco de Occidente.

**FINCA.** This is a private development organization (OPD) with an extensive rural credit operation covering 86 municipalities with a total of 21,000 clients.

**PILARH.** This Association is an OPD operating in Copán and Lempira with a highly regarded credit operation and some experience with land purchase and rural enterprise establishment.

Annex 12 provides more detailed information on the above three OPDs.

#### 4.2 Project management:

INA will establish the project management unit (UTA) through a contract with FAO-Honduras for consultant services. This arrangement will enable the PACTA to take advantage of established FAO practices in managing program funds and financial reporting, and therefore should facilitate an early start-up of project execution. The solution is particularly apt for the Pilot phase of the land access program, because it enables the focus to be placed on field operations, relations with the financial institutions, and facilitating establishment of the SEP. It also allows for the incubation, so to speak, of the UTA while the future institutional structure of PACTA evolves. If PACTA proves successful, it eventually may be established as an autonomous agency. It should be noted that FAO-Honduras has accumulated a great deal of valuable experience in rural development projects with an emphasis on natural resource management and land administration. Locally based FAO personnel bring a great deal of expertise to PACTA. They are regularly supported by Costa-Rica based and Chile regional office FAO land specialists. In addition to the PACTA, FAO is providing a Technical Cooperation Grant to GOH for technical assistance under a complementary TCA.

#### 4.3 Procurement issues:

There are no procurement issues to be resolved. All contracts will be small, apart from the contracting of FAO as the implementing agency, and community subprojects will be made as grants. Procurement will be based on the guidelines established in Annex 6. FAO will provide complementary administrative and technical services for which it will use funds from the IDA Credit not to exceed 7 % of the Credit value.

#### 4.4 Financial management issues:

**A. Financial management system.** The results of the financial assessment indicates that although FAO-Honduras has a financial management system that meets its needs, this system does not fully meet requirements to be able to generate project management reports (PMRs). As a result, a financial management action plan has been agreed with FAO-Honduras to achieve by credit effectiveness the certification of the project's financial management system with PMR capabilities, as required under the Bank's Loan Administration Change Initiative (LACI). In the event that by credit effectiveness FAO-Honduras does not yet have full PMR capabilities, it should at least have a system in place which the Bank's view meets minimum IDA requirements for financial management of the project. Conditions of effectiveness are: (a) hiring of the UTA staff who will handle financial management; (b) up-date of the project operations manual and the financial regulations for the land purchases and complementary subprojects; (c) design and implementation of a financial management system with PMR capabilities; and (d) hiring of the external auditors.

FAO-Honduras will be responsible for conducting annual project reviews, including audited financial statements of the project, as well as preparing periodic reports on physical and financial agreed project indicators. FAO-Honduras will prepare and transmit to IDA quarterly Project Management Reports (PMRs) that summarize project progress in terms of financial activity, key performance indicators, and procurement.

FAO-Honduras will maintain an adequate financial management system, compatible with Project Management Reporting (PMR) as required by IDA under the Loan Administration Change Initiative (LACI). The financial management system will include internal control systems, reliable records and report of project assets, accounting, financial reporting, physical and financial monitoring of project indicators, procurement management, reconciliation of the project records with the transfer of funds from IDA, and auditing systems—to ensure the provision of accurate and timely information to the World Bank regarding project resources and expenditures, in accordance with: (i) the Financial Accounting, Reporting, and Auditing Handbook (World Bank, 1995); (ii) the Bank's Operational Policy (OP) and Bank Procedure (BP) 10.02 dated July 1996; and (iii) the revised Bank financial management standards to comply with OP and BP 10.02, dated August 1997.

FAO-Honduras will be responsible for continuous project work plan updates to ensure consistency with the project's overall objectives, and project management according to best administration practices and the Bank's financial management and reporting requirements.

**B. Project Management Reports.** Under LACI introduced by the Bank in July 1998, FAO-Honduras should maintain a financial management system that integrates financial, physical and procurement activities of the project, and reported through PMRs. Disbursement of funds under the Credit will be through the traditional disbursement procedures, Statement of Expenditures (SOEs). Transition to PMR-based disbursements could be approved if requested by FAO-Honduras. The PMR will present a forecast for disbursements during the next six (6) months after the quarter being reported.

Independently from the disbursement procedure selected by FAO-Honduras, PMRs should be submitted to the Bank on a quarterly basis. These reports will be prepared 45 days after the end of each quarter. In addition, annual financial statements (to be included in the audit report) will be required.

**C. Annual Audits:** In addition to submission of quarterly PMRs, FAO-Honduras should contract an independent public accounting firm, to be hired by Credit effectiveness. The auditors should be hired, preferably under a multi-year contract (two years), according to terms of reference acceptable to the Bank, for the performance of annual project audits. The auditors will conduct interim audits through each year of project implementation. Costs of the external audits will be included in the technical assistance and services provided by FAO-Honduras. The project audited financial statements will be submitted to the Bank within 180 days of the close of the project's financial year. The Guidelines and Terms of Reference for Audit of Projects with Bank Financing by the World Bank in Latin America and the Caribbean Region should be followed when preparing the terms of reference for the external audit. The auditors should be hired before the commencement of the fiscal year to be audited. The terms of reference and the proposed short list of public accounting firms for the audit of the first project implementation year was submitted to the Bank at project negotiations, and the selected firm would be hired within 30 days of credit effectiveness.

**D. Flow of Project Funds.** IDA credit funds will be disbursed through FAO-Headquarters, from where the funds will be transferred to FAO-Honduras. FAO-Honduras will keep the funds in a separate bank account in US Dollars in a local commercial bank.

**E. Project Monitoring and Evaluation.** The project will be guided by bi-annual reviews of results, on which basis FAO-Honduras, INA, and IDA supervision missions will identify specific measures to: (i) address any areas of implementation weaknesses; and (ii) accommodate changes in priorities. These measures for improvement will be reflected in FAO-Honduras' proposal for the forthcoming year's project budget.

**D. Retroactive Financing.** Retroactive financing may be made on account of payments made for the eligible expenditures before Credit signing but after November 1, 2000 for consultants' services under the Technical Assistance and Administrative components of the Project in an aggregate amount not exceeding SDR 31,000 (US\$ 40,000 equivalent).

**5. Environmental:** Environmental Category: B (Partial Assessment)

5.1 Summarize the steps undertaken for environmental assessment and EMP preparation (including consultation and disclosure) and the significant issues and their treatment emerging from this analysis.

Preparation studies included analysis of the environmental impacts of the program. In general, the impacts are positive: the project will provide access to land for poor, rural producers and thereby contribute to the reduction in slash and burn agriculture by landless farmers and upland farmers migrating to marginal, public lands, as well as provide an incentive to landowners practicing extensive, but low return agriculture or livestock rearing to sell land to participating groups of rural producers. The enterprise business plans and farm models would include land and water management practices that would contribute to watershed stabilization and erosion control.

5.2 What are the main features of the EMP and are they adequate?

NA

5.3 For Category A and B projects, timeline and status of EA:

Date of receipt of final draft: 5/27/1999

The farm and productive activities that would be eligible for financing were subject to environmental analysis. Models include environmental standards for soil and moisture conservation, land management, and water management. Resettlement is not an issue, as clear private land title is a prerequisite for land sales.

The project promotes production models that are economically viable and which contribute to the rational use and conservation of natural resources and hence are sustainable in the long term. Two of the five prospective UTLs already have begun to measure the economic value of environmental services, like soil and water conservation. (For example, the hidden cost of the losses due to slash and burn of 1 hectare in the department of Lempira was estimated by one of the prospective UTLs at \$396 per year.) The UTLs will incorporate this type of analysis in the Participatory Monitoring and Evaluation system.

5.4 How have stakeholders been consulted at the stage of (a) environmental screening and (b) draft EA report on the environmental impacts and proposed environment management plan? Describe mechanisms of consultation that were used and which groups were consulted?

The social assessment included an environmental analysis and consultations with samples of potential beneficiaries, focus group interviews with potential beneficiaries in different regions, and review of the social analysis carried out by the PAAR Rural Land Management Project (IDA Credit 2940-HO) for the design and promotion of the Upland Fund for Rural Producers. Government consulted with the major producer associations and with NGOs providing technical assistance and capacity building to rural producers. Several workshops were held to discuss the planned design with producer organizations, other

international donors, NGOs, and Government.

5.5 What mechanisms have been established to monitor and evaluate the impact of the project on the environment? Do the indicators reflect the objectives and results of the EMP?

Business plans include environmental indicators, and the monitoring and evaluation indicators include sustainability of the farm models in terms of land and water management. Given that the beneficiaries are likely to use labor intensive farming systems, also moving away from extensive cattle rearing and other uses common to larger land owners, environmental improvements are expected from a change in land use to more productive and labor-intensive technologies.

## **6. Social:**

6.1 Summarize key social issues relevant to the project objectives, and specify the project's social development outcomes.

A social assessment was performed using a participatory methodology in the areas proposed for the pilot phase of PACTA. The objectives of the assessment were to i) analyze the viability of the proposed implementation scheme in all its aspects; ii) help to define the roles of the respective actors in the process; iii) identify the needs of beneficiaries to participate effectively and to examine in particular the concept of a productive enterprise where individual ownership and choices have to be reconciled with need to take actions and decisions as a group; and iv) make recommendations about an appropriate methodology for participatory project monitoring and evaluation consistent with the decentralized and demand-driven design of the program. Establishment of a land fund program has been a long standing demand of peasant organizations in Honduras. Although some groups had hopes that Government would create a separate, public fund for land purchase, a broad-based acceptance has been obtained through the preparation work and the related dialogue with civil society led by INA. In addition, the social assessment included consultations in sample regions where the program will be carried out, which detected a widespread interest among both members of main peasant organizations and other small producers and rural poor.

**1. Individual ownership and the enterprise.** The social assessment has endorsed a beneficiary arrangement whereby group members would self-select the desired form of association, property and system of production. The basic criterion for establishing the enterprise is that it be legally constituted to enter into credit contracts and purchase-sale agreements. A legal analysis has been conducted to outline the options available under Honduran law for groups to acquire property and assure property rights to each member. The options available – and the internal regulations adopted by each group – would determine how property rights are assigned within the enterprise; how responsibility for loan repayment is managed; whether or not collective areas are established initially; and so on. An explanation of the options and the procedures to implement each one will be incorporated in the Operations Manual.

**2. Legal services and Organization Support.** The social assessment showed clearly that legal services and organizational support will be equally as important as technical services related to production and commercialization.

**3. Size of Effective Groups.** The groups likely to participate in PACTA are likely to have from 8 to 20 families; be experienced in agriculture; possibly have participated in other aspects of a local rural development program, as in the example of the Caja Rural or programs focused on appropriate technology. Other participants would include producers decapitalized as a result of Mitch, producer organizations without land, participants in local development programs, or, as in the case of PILARH, groups that have not necessarily worked together before for any purpose, although they may have had other group experiences. The groups must be willing to formally accept training related to enterprise formation. Members should reside in the same vicinity where the rural enterprise is to be established.

**4. Women's participation.** The role of women in rural development projects is increasingly important in Honduras. The social assessment found that many groups of women are already formed for different purposes and are likely to be candidates for land purchase. The assessment noted that "Women's skills as administrators, high level of responsibility with respect to obligations, and seriousness in their work [as participants in rural development projects] indicate that women will play an important role in PACTA."

**5. Participatory Monitoring and Evaluation.** M&E will focus on three aspects: (a) operational procedures used in the pilot; (b) social and economic impacts of the program; and (c) institutional learning of UTLs and UTA to improve pilot activities and evaluate results. All stakeholders will be involved in defining objectives and indicators, and reviewing the information generated. The UTA will have budget for the studies involved and carry out this component through the UTLs. Producers can provide feedback on the effectiveness of UTA and UTL relations through this M&E method.

6.2 Participatory Approach: How are key stakeholders participating in the project?

a. Primary beneficiaries and other affected groups:

Producer organizations will be assigned 3 of the 9 positions on the Consejo Directivo of PACTA (mandated in Acuerdo 893-00). At the local level, members of groups that decide to participate in PACTA will be self-selected, and all likely to be rural producers with entrepreneurial skills. Selection of land and negotiation of the purchase price will also be in the hands of the producer groups. The structure of the enterprise, form of property, and production model will be self-determined. These decisions, however, have to take into account existing law and the comfort of the lending institution with different choices. In relation to the options for investment, the Operations Manual will specify only the kind of activities not permitted (repayment of other debt, activities that degrade the environment, etc.); and kinds of land that are ineligible for financing (urban land, land in dispute, etc.).

b. Other key stakeholders

**Financial institutions:** Both the regulations and operational procedures reflect numerous modifications introduced as a result of discussion with the financial institutions. A dialogue about the proposal began in the earliest stages.

6.3 How does the project involve consultations or collaboration with NGOs or other civil society organizations?

**Local technical units:** All aspects of the proposal were developed in concert with the prospective UTL, from the initial concept to the analysis that determined cost of services.

6.4 What institutional arrangements have been provided to ensure the project achieves its social development outcomes?

Strong technical assistance has been included in the activities of the UTLs and the Coordination Unit (UTA) and participatory monitoring and evaluation will generate periodic feedback from pilot beneficiaries.

6.5 How will the project monitor performance in terms of social development outcomes?

Performance indicators include attention to gender, group formation, sustainability of producer groups, and organizational skills and capacity building. Field UTLs have long-term experience with social development in their regions of operation.

## 7. Safeguard Policies:

7.1 Do any of the following safeguard policies apply to the project?

Policy	Applicability
Environmental Assessment (OP 4.01, BP 4.01, GP 4.01)	<input checked="" type="radio"/> Yes <input type="radio"/> No
Natural habitats (OP 4.04, BP 4.04, GP 4.04)	<input type="radio"/> Yes <input checked="" type="radio"/> No
Forestry (OP 4.36, GP 4.36)	<input type="radio"/> Yes <input checked="" type="radio"/> No
Pest Management (OP 4.09)	<input checked="" type="radio"/> Yes <input type="radio"/> No
Cultural Property (OPN 11.03)	<input type="radio"/> Yes <input checked="" type="radio"/> No
Indigenous Peoples (OD 4.20)	<input type="radio"/> Yes <input checked="" type="radio"/> No
Involuntary Resettlement (OD 4.30)	<input type="radio"/> Yes <input checked="" type="radio"/> No
Safety of Dams (OP 4.37, BP 4.37)	<input type="radio"/> Yes <input checked="" type="radio"/> No
Projects in International Waters (OP 7.50, BP 7.50, GP 7.50)	<input type="radio"/> Yes <input checked="" type="radio"/> No
Projects in Disputed Areas (OP 7.60, BP 7.60, GP 7.60)	<input type="radio"/> Yes <input checked="" type="radio"/> No

7.2 Describe provisions made by the project to ensure compliance with applicable safeguard policies.

See discussion of EA analysis above.

## F. Sustainability and Risks

### 1. Sustainability:

The project design provides a strong guarantee of long-term sustainability. The pilot involves the private financial sector from the beginning, and other financiers are likely to enter the program by about the third year. Because the approval of beneficiary producers is by the private sector bank, there is no dependency on Government for creation of a separate lending facility/program.

The use of existing project technical assistance units (UTLs) in the regions where the pilot will be implemented eliminates the need to create new project administration units and builds on the strength of successful programs at the local level. The technical assistance component of the subprojects will be coordinated with the Upland Fund for Rural Producers (financed under the Rural Land Management Project, Cr. 2940-HO), helping to ensure the long-term quality of the implementation of the business plans. Sustainability of the farm models from an economic perspective has been summarized under E3; and the basis of environmental sustainability is noted under E6.

The self-selection of group members for accessing the program is another factor for sustainability. For example, the group will more likely achieve long term stability if its members are self-selected and come from the same community. This has absolutely been demonstrated in the case of PILARH, the pilot land access program in Copan region.

**2. Critical Risks** (reflecting the failure of critical assumptions found in the fourth column of Annex 1):

<b>Risk</b>	<b>Risk Rating</b>	<b>Risk Mitigation Measure</b>
<p><b>From Outputs to Objective</b></p> <p>Official commitment to the program cannot be maintained through the pilot cycle.</p> <p>Civil society perceives program as a substitute for alternative forms of land reform.</p> <p>External factors, natural disasters, affect viability of the business plans.</p>	<p>N</p> <p>S</p> <p>M</p>	<p>Attention has been paid in preparation to gaining commitment from government, civil society, and producers' organizations, and to developing a suitable legal framework for the pilot.</p> <p>Continued dialogue with civil society and participatory monitoring and evaluation.</p> <p>Flexibility in the model to address payment issues as they arise and seek solutions; annual performance reviews will focus particularly on financial sustainability of enterprises.</p>
<p><b>From Components to Outputs</b></p> <p>Financial institutions are unable to provide adequate long-term financing.</p> <p>As clients and products are new, default rate is higher than expected creating a lack of confidence among financial institutions.</p> <p>There is not adequate quality control of the business plan proposals by the UTLs.</p> <p>UTLs are not sufficiently motivated to provide quality technical assistance.</p>	<p>S</p> <p>M</p> <p>M</p> <p>N</p>	<p>Financial analysis has been made of potential institutions and the project dimensioned to not require large amounts of land credit.</p> <p>Supervision by consultants and technical assistance oversight has been built into the agreement with FAO to bring international expertise during implementation.</p> <p>Social and economic assessment has identified potential areas of risk; pilot experience of PILARH has been drawn upon.</p> <p>Only UTLs with proven track record in the field have been selected, and payments for services will be tied to performance.</p>
<b>Overall Risk Rating</b>	S	

Risk Rating - H (High Risk), S (Substantial Risk), M (Modest Risk), N(Negligible or Low Risk)

**3. Possible Controversial Aspects:**

No significant political or social controversies are expected to be generated by the project. However, the project incurs risks simply because access to land is already a sensitive issue and expectations in civil society are high regarding the portion of the rural poor that the program should be able to assist.

**G. Main CreditConditions**

**1. Effectiveness Condition**

1. Approved Financial Regulations and Operational Manual.
2. Legal Opinion and Approval of Credit Agreement by Congress.
3. Agency contract with FAO has been signed.
4. That an adequate financial management system for the project has been implemented within

FAO-Honduras which is acceptable to the World Bank, and includes procedures for its operation and maintenance during project implementation.

5. Participation Agreement with at least one participating Financial Institution has been signed.
6. Qualified personnel, acceptable to the World Bank, for the management of the projects.
7. External auditors have been selected.
8. Subsidiary Agreement signed between GOH and INA.

**2. Other** [classify according to covenant types used in the Legal Agreements.]

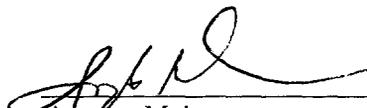
1. Condition of Disbursement: No subgrant will be disbursed unless Beneficiary has acquired legal title to land finance with a portion of a subloan and corresponding subgrant agreement has been signed. (see Paragraph 3(b) of Schedule 1 of the DCA.)

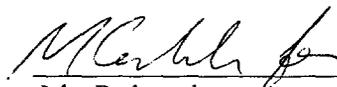
**H. Readiness for Implementation**

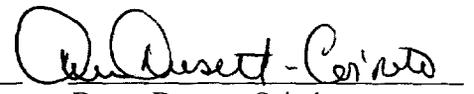
- 1. a) The engineering design documents for the first year's activities are complete and ready for the start of project implementation.
- 1. b) Not applicable.
- 2. The procurement documents for the first year's activities are complete and ready for the start of project implementation.
- 3. The Project Implementation Plan has been appraised and found to be realistic and of satisfactory quality.
- 4. The following items are lacking and are discussed under loan conditions (Section G):

**I. Compliance with Bank Policies**

- 1. This project complies with all applicable Bank policies.
- 2. The following exceptions to Bank policies are recommended for approval. The project complies with all other applicable Bank policies.

  
Augusta Molnar  
Team Leader

  
John Redwood  
Sector Manager

  
Donna Dowsett-Coirolo  
Country Manager

**Annex 1: Project Design Summary**  
**HONDURAS: Access to Land Pilot Project (PACTA)**

<b>Hierarchy of Objectives</b>	<b>Key Performance Indicators</b>	<b>Monitoring &amp; Evaluation</b>	<b>Critical Assumptions</b>
<p><b>Sector-related CAS Goal:</b> Increased access to land and credit in rural areas.</p>	<p><b>Sector Indicators:</b> Improved land markets and increased access of rural smallholders to land and credit.</p>	<p><b>Sector/ country reports:</b></p>	<p><b>(from Goal to Bank Mission)</b></p>
<p><b>Project Development Objective:</b> The objective of the Land Access Pilot Program (PACTA) is to support the acquisition of land and the formation of sustainable farm enterprises by self-organized landless and land-poor peasant families, increasing private sector lending for this purpose.</p>	<p><b>Outcome / Impact Indicators:</b> About 1600 farm families participate in local land markets and establish sustainable land-based enterprises.  Private financial institutions increase lending for land purchases by small farmers.  Increased incomes through land productivity and output in project sites.  Decentralized model for land access tested.</p>	<p><b>Project reports:</b></p>	<p><b>(from Objective to Goal)</b>  Official commitment to the program is maintained through the pilot cycle.  Civil society perceives program as a substitute for land regularization and demands land reform.</p>
<p><b>Output from each Component:</b>  1. UTL hired and able to provide (or facilitate) quality technical and legal services within established cost guidelines.  2. Financial institutions develop appropriate methodology to deliver credit products to target population; and devote sufficient resources to fund all qualified sub-projects.  3. Participant families able to negotiate land purchase, establish legal structure, enter into credit contracts, and develop new enterprises.</p>	<p><b>Output Indicators:</b>  Groups of loan candidates receive adequate technical and legal services to prepare and implement viable proposals and identify land for purchase.  Seventy-five percent of families identified as eligible by UTLs receive Bank financing and financial institutions continue to allocate resources for this program.  A majority of groups participating in the project are able to pay off land purchase loans and maintain viable enterprises.</p>	<p><b>Project reports:</b></p>	<p><b>(from Outputs to Objective)</b>  There is adequate quality control of the business plan proposals by the UTLs.  UTLs are sufficiently motivated to provide quality technical assistance.  Financial institutions have an availability of long-term financing.  Default rate is not higher than expected creating confidence among financial institutions.  External factors, natural disasters, do not affect viability of the business plans.  Groups remain organized.</p>

4. PACTA is established as a national program and operates in conformity with the tested implementation model.	Pilot evaluation leads to endorsement of expansion of program and donor or national financing is available for complementary subprojects in Year 4.	Monitoring and evaluation reports Participatory M&E	Flexible implementation allows adjustments in pilot scope and operation as the experience unfolds.
<b>Project Components / Sub-components:</b> Technical and Legal Assistance to Rural Producers Land Purchases  Complementary Subprojects  Project Administration	<b>Inputs: (budget for each component)</b> US\$ 1.17 million  US\$ 6.84 million  US\$ 7.16 million  US\$ 2.10 million	<b>Project reports:</b>  Financial management reports  Private sector institution reporting and UTLs reports  Financial management reports  Supervision missions by Government, FAO and the World Bank	<b>(from Components to Outputs)</b> UTLs provide services as planned Financial sector institutions have the liquidity and interest to provide land financing Resources are available and disbursed in a timely manner Qualified staff are available for the administrative positions.

**Annex 2: Detailed Project Description**  
**HONDURAS: Access to Land Pilot Project (PACTA)**

**By Component:**

**Project Component 1 - US\$1.17 million**

**Technical and Legal Assistance to Rural Producers**, includes consultant services from local technical units (UTLs), which include existing project administration units of regionally-based rural development programs in the project area. UTLs will provide legal services and technical assistance in the formulation and implementation of business plans for potential beneficiaries who identify lands for purchase and development. UTLs will promote the PACTA in their regions of operation, providing publicity and information services regarding the program, qualification of groups eligible for TA that identify land for sale and meet the criteria to propose viable business plans, assistance in assessing land market values, and in preparation of business plans for subprojects. Much of this TA will draw on successful experiences by small farmers in these regions. Legal services provided by UTLs or consultants contracted by them can include assistance in concluding the purchase-sale agreement for land and assistance in obtaining legal data on the property prior to purchase. In the first phase of assistance, UTLs will receive remuneration for services provided on a per-family basis (50% of the maximum dollar amount per family which is US\$ 224 equivalent) upon initiating activities with an eligible group of loan candidates. The balance would be paid in the event that the group is approved for financing by a private sector financial institution participating in Component 2. In the phase after loan approval, the newly established enterprise would be eligible for two years of technical assistance from the UTL and/or another private service provider, consistent with the guidelines of the Upland Producer's Fund of the Rural Land Management Project, up to a maximum amount of \$ 225/year/family. In this phase, services can include organizational support (financial or administrative management) and technical services related to production and commercialization activities in the group's business plan.

**Project Component 2 - US\$6.84 million**

**Land Purchase subloans** include the financing provided to groups of loan candidates by participating private sector financial institutions. Financial institutions that qualify according to eligibility criteria summarized in Annex 12 will provide all funds for land purchase, and other investments as needed, in the framework of PACTA. The beneficiaries would be groups of small rural producers eligible for loan financing, who would agree to follow a group business plan for the land, with the option of operating the farm as independent parcels when the loan is completely repaid, or continuing to operate the land through a cooperative group arrangement. The financial regulations and procedures were established parting from a conceptual scheme that proved of interest to several institutions, including banks, credit cooperatives, and other credit providers. Interest on the part of these institutions has been stronger than initially expected; and two representatives of the financial sector have agreed to participate on the Board of Directors of PACTA in the expectation of providing significant amounts of loan financing to eligible groups of loan candidates.

**Project Component 3 - US\$ 7.16 million**

**Complementary Subproject Grants** includes support for formation of viable enterprises by means of subproject grants for fixed and working capital investments within a comprehensive business plan for land purchase and productive enterprises. The grants for subprojects will be managed so that beneficiaries of the land purchases have strong incentives to repay the land purchase loan. Only those groups who are approved for a land purchase loan and have acquired title to the land purchased (component 2) would be eligible for the complementary subproject grants.

The maximum total grant to a family would not exceed 45 percent of the total value of the farm business plan, which itself includes the value of land, fixed, and working capital (some of which may be included in the FI loan), and beneficiary contributions in cash or kind. Project design envisages an absolute ceiling of \$ 3,500 per family for the grant (See Annex 12 for more details on the financial regulations.) The actual amounts assigned under the program per beneficiary group would be adjusted as a function of the need for investment capital and the capacity of group members to repay at different stages of the development of the farm.

Transfer of the grants to beneficiaries would be in two parts: (a) an initial transfer of no more than 70% of the value of the productive investments (within the 45% ceiling) to the group's account, to be released as needed; (b) a transfer of the 30% of the value of the productive investments to a fixed-term CD, which upon maturity would be available to the producer groups with a good loan repayment history during this period.

#### **Project Component 4 - US\$2.40 million**

**Project Administration** includes the management of the PACTA pilot by a coordination unit team of consultants, recruited and supervised by the Food and Agricultural Organisation of the United Nations (FAO). The team would have resources for additional consultant services for special evaluation and feasibility studies, monitoring and evaluation, and supervision. The coordination unit (UTA) would have six functions: (a) financial management and reporting; (b) other administrative and legal business of PACTA, such as entering into agreements with the local UTLs and establishing formal working agreements with the financial institutions; (c) support for the local UTLs, including coordination of training and information exchange among the UTLs and financial institutions and normalizing of forms, contracts, and reports; (d) coordination of standard monitoring and evaluation of progress in relation to the quantitative indicators of the Project; and (e) quality control, both monitoring and evaluation with local participation, and review of compliance with rules of eligibility and "best practices" established in the pilot.

The activities of the UTA would be overseen by an Advisory Board, consisting of Government, private sector financial institutions, peasant organizations, NGOs, and international donor representatives with related programs.

The operational manual includes a system of participatory follow-up and evaluation (Seguimiento y Evaluacion Participativa-SEP), additional to the normal monitoring and reporting of the UTA. SEP refers to a *systematic* approach to learning lessons and incorporating them into the pilot phase and preparing for its possible expansion. All actors – participating families, financial institutions, UTLs and the Coordinating Unit – would be included in the system to i) better comprehend the impact of the program; ii) analyze the adequacy of the rules and processes initially designed; and iii) assure that the lessons learned are incorporated as the project is being implemented. The SEP would analyze at least three fundamental working relationships between: a) the UTA and the UTL, hired to carry out the program in the different regions; b) the UTL local committees (CLA), other service providers, and the newly formed enterprises; and c) UTA and the financial institutions.

**Annex 3: Estimated Project Costs**  
**HONDURAS: Access to Land Pilot Project (PACTA)**

<b>Project Cost By Component</b>	<b>Local US \$million</b>	<b>Foreign US \$million</b>	<b>Total US \$million</b>
Technical and Legal Assistance to Rural Producers	1.05	0.12	1.17
Land Purchase	6.84	0.00	6.84
Complementary Subprojects	7.16	0.00	7.16
Project Administration	0.78	0.83	1.61
<b>Total Baseline Cost</b>	15.83	0.95	16.78
<b>Physical Contingencies</b>	0.14	0.06	0.20
<b>Price Contingencies</b>	0.00	0.02	0.02
<b>Total Project Costs</b>	15.97	1.03	17.00
<b>Total Financing Required</b>	15.97	1.03	17.00

**Annex 4**  
**HONDURAS: Access to Land Pilot Project (PACTA)**  
**Economic Analysis Summary**

**Introduction**

While PACTA would produce a variety of benefits associated with more efficient land markets, the economic and financial analyses focus on production improvements from farms participating in the project. Through technical assistance and complementary sub-projects, net benefits from farm production will increase. These increased net benefits form the basis for the economic analysis. A complementary financial analysis ensures that these farm models generate the necessary flow of net benefits to service their debt obligations. Taken together, the economic and financial analyses show that the farm models are financially viable and produce economically significant net benefits.

Given the decentralized nature of working through UTLs, it is not possible in advance to specify how project resources will be allocated across different regions and productive systems. Therefore, while the economic and financial analyses are based on farm models from a range of agro-ecological conditions expected to be encountered during implementation of the project, it is not possible to aggregate these farm models into a cost-benefit analysis for the entire project. Instead, cost-benefit analyses are conducted for individual farm models which incorporate the technical assistance and administrative costs associated with the project.

**Farm Models**

In order to assess the economic and financial viability of the proposed project, the FIs and the preparation team took the most appropriate existing farm models for upland agriculture (from research funded by FAO) and applied the rules of PACTA. For each farm model, data was assembled on production, recurrent and investment costs and the estimated market value of land. In addition, in each model, data was collected on with and without project scenarios. The without project models are characterized by subsistence agriculture, with minimal improvements and are not meant to be viable investments within the PACTA program. Instead, these without project models are used in the economic analysis to determine the economic net benefits of the project. The with project models, which are characterized by greater investment, are used in the financial analysis to show that, combined with the complementary sub-projects, they are capable of generating sufficient net farm revenues to meet debt payment obligations.

*Table 1. Farm Model Characteristics*

<b>Farm Model Name</b>	<b>Region</b>	<b>Farm Size (manzanas)</b>	<b>Products</b>
1. Ganaderia en Tropico Seco	Pacific Slope	6	leche, ternero, vaca, cerdo, huevos, pollos, gallinas, maiz, maicillo, tuza, lena, postes, postoreo
2. Agroforestal con Maiz-Frijol	Pacific Slope	2	frijol, maiz, tuza, lena, postes, postoreo
3. Ganaderia en Tropico Humido	Atlantic Coast	5	carne, leche

**Economic Analysis: Cost-Benefit Analysis of the Farm Models**

Three different cost-benefit analyses were conducted for each of the three farm models. First, the net present value (NPV) and internal rate of return (IRR) were calculated considering only the on-farm revenues and recurrent and investment costs. Second, the per-family technical assistance provided by the UTLs was added to the "with project" costs (the UTLs provide US\$225 per family in sub-project development TA and US\$230 per family for two years of sub-project management TA). Third, the

per-family administrative costs for managing the proposed project were also added to the "with project" costs (the per-family administrative costs are: US\$336 in year one, US\$314 in year 2, and US\$237 in year 3). Since the last case incorporates all of the costs associated with the project, it represents a farm level economic analysis of the project. The results from these calculations are presented in Table 2.

*Table 2. Farm model economic analysis*

<b>Farm Model/Costs Included</b>	<b>NPV (US dollars)</b>	<b>IRR (percent)</b>
1. Ganaderia en Tropicico Seco		
a. on-farm investment costs only	1,800	17
b. with technical assistance costs	1,200	14
c. with technical assistance and administrative costs	430	11
2. Agroforestal con Maiz-Frijol		
a. on-farm investment costs only	2,263	28
b. with technical assistance costs	1,663	20
c. with technical assistance and administrative costs	893	14
3. Ganaderia en Tropicico Humido		
a. on-farm investment costs only	1,393	16
b. with technical assistance costs	793	13
c. with technical assistance and administrative costs	23	10

Note: All net present values are calculated at a 10 percent discount rate.

The results in Table 2 show that in all cases, the farm models are characterized by positive net present values at a nine percent discount rate. When considering on-farm investment costs only, the IRR for the three models range from 16 to 28 percent. When the cost of technical assistance is included, the IRR range from 13 to 20 percent. Finally, when all project costs are added (technical assistance and administrative), the IRR range from 10 to 14 percent. Unfortunately, the aggregate nature of the data set limit the ability to conduct sensitivity analysis on these results.

#### **Financial Analysis of the Farm Models**

The financial viability of the three farm models (with project technologies) was also assessed (see Table 3 for additional financial data on the three models). The financial analysis for these three farm models assumes a 30 percent interest rate, a 10 year repayment period with one year grace period, 18 percent inflation rate, and a 25 percent interest rate on bank savings accounts (see Table 3 for additional information). The financial analysis demonstrates that these models are appropriate examples for the PACTA program since their investments generate sufficient net farm revenues to cover debt payments, and the value of the complementary sub-projects does not exceed the planned US\$3,500 ceiling.

*Table 3. Financial analysis farm model data*

Farm Model	land cost	total investment	family contribution	commercial bank loan	complementary sub-project
1. Ganaderia en Tropicico Seco	2,700	3,500	160	6,040	2,340
2. Agroforestal con Maiz-Frijol	2,800	1,000	50	3,750	1,620
3. Ganaderia en Tropicico Humido	7,500	3,250	200	10,550	3,500

The financial analysis assumes that the commercial bank loan will be paid back over ten years with a one year grace period. Farmers use the complementary sub-projects to finance working capital and fixed investments required in the farm model's business plan. In the base case, the complementary sub-projects were disbursed as follows: 20 percent in year 0; 25 percent in year 1; 25 percent in year 2; and 30 percent in year 3. Farmers then use the real net farm revenues (net after using sub-project disbursements to pay for

working capital) to make the required loan payments. If, in the early years of loan repayment, net farm revenues are greater than the loan payment (e.g., during the grace period), it is assured that the difference is saved to make loan payments in later years.

*Table 4. Financial analysis of the farm models*

Farm Model/Financial Flow	1	2	3	4	5	6	7	8	9	10	11
1. Ganaderia en Tropicico Seco											
a. debt service (real)	0	1,683	1,426	1,209	1,024	868	736	623	528	448	379
b. net farm revenues w/ sub-proj.	90	465	1,773	1,365	1,219	1,069	1,069	1,069	1,069	1,244	1,071
c. real cash flow	90	90	109	156	195	201	333	446	541	797	691
2. Agroforestal con Maiz-Frijol											
a. debt service (real)	0	1,035	877	743	630	534	452	383	325	275	233
b. net farm revenues w/ sub-proj.	100	1,135	977	932	859	753	753	753	753	1,025	1,014
c. real cash flow	100	100	100	189	230	220	301	370	429	749	781
3. Ganaderia en Tropicico Humido											
a. debt service (real)	0	2,975	2,521	2,136	1,810	1,534	1,300	1,102	934	791	671
b. net farm revenues w/ sub-proj.	50	3,026	2,571	2,186	1,916	1,908	1,754	1,658	1,658	1,658	1,135
c. real cash flow	50	51	50	50	106	374	454	556	724	867	464

Table 4 shows that all three farm models produce sufficient financial flows to cover 100 percent of their debt service payments in all periods. Again, the aggregate nature of the data set makes it difficult to conduct sensitivity analysis on these results. However, after adjusting the profile of the sub-project disbursements to 50 percent in year 0, 20 percent in year 2, and 30 percent in year 3, models 1 and 2 are still financially viable while model 3 has a negative real cash flow in year 2 of US\$115.

**Annex 5: Financial Summary**  
**HONDURAS: Access to Land Pilot Project (PACTA)**

Years Ending  
December 31

	IMPLEMENTATION PERIOD						
	Year 1	Year 2	Year 3	Year 4	Year 5	Year 6	Year 7
<b>Total Financing Required</b>							
<b>Project Costs</b>							
Investment Costs	4.3	6.1	6.6	0.0	0.0	0.0	0.0
Recurrent Costs	0.0	0.0	0.0	0.0	0.0	0.0	0.0
<b>Total Project Costs</b>	4.3	6.1	6.6	0.0	0.0	0.0	0.0
<b>Total Financing</b>	4.3	6.1	6.6	0.0	0.0	0.0	0.0
<b>Financing</b>							
IBRD/IDA	2.1	2.9	3.0	0.0	0.0	0.0	0.0
Government	0.1	0.1	0.4	0.0	0.0	0.0	0.0
Central	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Provincial	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Co-financiers	0.0	0.0	0.0	0.0	0.0	0.0	0.0
User Fees/Beneficiaries	0.4	0.6	0.6	0.0	0.0	0.0	0.0
Others	1.7	2.5	2.6	0.0	0.0	0.0	0.0
<b>Total Project Financing</b>	4.3	6.1	6.6	0.0	0.0	0.0	0.0

Main assumptions:

## **Annex 6: Procurement and Disbursement Arrangements**

### **HONDURAS: Access to Land Pilot Project (PACTA)**

#### **Procurement**

Procurement of goods financed by the Bank under the proposed project will be carried out in accordance with the Bank's *Guidelines: Procurement under IBRD Loans and IDA Credit*, published in January 1995 (revised January/August 1996, September 1997 and January 1999). Consultant services will be procured in accordance with the *Guidelines: Selection and Employment of Consultants by World Bank Borrowers* published in January 1997 (revised in September 1997 and January 1999), and the provisions stipulated in the Credit Agreement.

#### **Procurement Responsibilities and Capacity**

The project will support a government pilot program that will be cofinanced by private financial institutions to provide access to rural finance to producers. For this purpose, the Government and FAO have agreed to work together to implement a pilot project that will test an approach to provide credit to producers eligible for loan financing.

For the implementation of the project, the Government plans to contract FAO to establish a coordinating unit (UTA) in INA that will be in charge of the financial management and reporting system, the legal business with the financial institutions, training of UTLs and financial institutions in the use of standard forms and contracts, monitoring and evaluation of the progress indicators of the project, and quality control. This unit will be comprised of consultants who will be hired with the credit proceeds. FAO-Honduras also plans to charge for additional administrative and technical support services, up to an amount not to exceed 7% of the Credit. FAO will separately cover the office expenses for the UTA.

Justification of sole-source. The Government justification for sole-source contracting of FAO is based on FAO's unique and long experience in Honduras with promoting and implementing programs for decentralized rural development schemes, such as that contemplated in the PACTA (agricultural and forestry extension, training and capacity-building at municipal level and among producer groups, micro-credit and financial intermediation, and decentralized project administration). FAO-Honduras has experience in building capacity within Government and civil society and in providing technical assistance to address issues with controversial political and social content, such as land and watershed management. FAO also counts with a unique, specialized unit in Rome that provides technical assistance to various donors and country clients on land administration, land reform, and pilots on market-assisted land reform in Latin America and other geographic regions. Some of these specialists would be made available in special assignments to the project, such as staff in the regional field office and in Rome. The Government strongly believes that, at this point, the project success will depend on having a neutral but highly qualified party to manage the pilot, since the objective is to test a model, but not create a separate agency.

For implementing the project and administering the funds, FAO fee would be 7 % of the total credit amount over a three year period. FAO will in turn provide:

Description of Support Services from FAO	Percentage	Equivalent in US\$
Technical support from headquarters and Santiago de Chile, assigning senior staff to the project, mainly from the Policy and Rural Development Divisions	1.50%	112,150
Technical and administrative support from FAO Honduras	1.50%	112,150
Preparation of technical and administrative reports	0.75%	56,075
Technical and financial audits	1.25%	93,458
Administrative overhead including accounting, procurement service and communications	1.50%	112,150
Headquarters (Rome) overhead	0.50%	37,383
Total	7.00%	523,364

For procurement of goods and consultant services, FAO will follow IDA's procurement guidelines and standard documents for competitive selection.

An action plan has been agreed with FAO-Honduras to ensure that it has the required procurement capacity. The UTA will include a manager, financial and operations supervisors, a procurement officer with experience in IDA operations, and a monitoring and evaluation officer, and one assistant. The UTA should have a clear definition of roles and responsibilities with regard to procurement, i.e. approvals, supervision, reporting, etc.; maintain appropriate procurement files and file control system; and have an adequate monitoring control system. This will be a chapter of the Operational Manual and the Agency Agreement between GOH and FAO-Honduras. The establishment of this Unit is a condition of effectiveness.

In addition, FAO-Honduras has developed a Technical Cooperation Project (TCP) for US\$ 280,000 to provide complementary technical assistance to Government of Honduras related to the monitoring of the pilot PACTA project. This consists of international experts who will carry out or oversee evaluation studies and field research, as well as expertise on similar programs from other regions. This is additional to the technical services described in the table above.

#### **Procurement Arrangements**

a) Goods. No ICB is expected in this project. Goods to be procured will consist of two vehicles and office equipment. The vehicles are estimated to cost approximately US\$60,000 and will be procured following NCB procedures. The amount estimated for office equipment is US\$20,000 and will be procured following shopping procedures in accordance with paragraphs 3.5 and 3.6 of the Guidelines.

b) Consulting Services. (US\$ 2.92 m) The project will finance technical and legal assistance to rural producers. As part of this activity the project proposes to finance as consultant services local technical units (UTLs), mostly under NGO management, that are already providing this type of services to producers. These services cover legal assistance, formulation and implementation of business plans for

potential beneficiaries, information services about the program, organizational support, and production and commercialization activities. These UTLs, which are NGOs, will be hired as consulting firms using QCBS procedures or Consultant Qualifications depending upon the size of the contract. Selection is on the basis of qualifications, since all UTLs will be paid a fixed cost set on a per family basis, for the technical assistance provided to producer groups (see project description). Individual consultants will be hired to support the coordinating unit team of consultants who will be managing the pilot project with FAO, up to an aggregate amount of US\$490,400. In addition, FAO services will be contracted as consulting services.

c) Complementary Subprojects. These subprojects consist of grants for fixed and working capital investments to beneficiaries of land purchases. The Operational Manual and its *Reglamento Financiero* will describe in detail the eligibility criteria, procedures, and amounts of the grants. The maximum amount per family is US\$3,500. IDA will cover 100% of the subproject grants net of any local tax obligations incurred. A summary of this information is included in Annex 12.

**Procurement methods (Table A)**

**Table A: Project Costs by Procurement Arrangements**  
(US\$ million equivalent)

Expenditure Category	Procurement Method <sup>1</sup>			N.B.F.	Total Cost
	ICB	NCB	Other <sup>2</sup>		
<b>1. Works</b>	0.00 (0.00)	0.00 (0.00)	0.00 (0.00)	0.00 (0.00)	0.00 (0.00)
<b>2. Goods</b>	0.00 (0.00)	0.06 (0.05)	0.02 (0.02)	0.00 (0.00)	0.08 (0.07)
<b>3. Services</b>	0.00 (0.00)	0.00 (0.00)	2.64 (2.34)	0.28 (0.00)	2.92 (2.34)
<b>4. Subprojects</b>	0.00 (0.00)	0.00 (0.00)	7.16 (5.59)	0.00 (0.00)	7.16 (5.59)
<b>5. Commercial loans</b>	0.00 (0.00)	0.00 (0.00)	0.00 (0.00)	6.84 (0.00)	6.84 (0.00)
<b>6. Recurrent costs</b>	0.00 (0.00)	0.00 (0.00)	0.00 (0.00)	0.00 (0.00)	0.00 (0.00)
<b>Total</b>	0.00 (0.00)	0.06 (0.05)	9.82 (7.95)	7.12 (0.00)	17.00 (8.00)

<sup>1/</sup> Figures in parenthesis are the amounts to be financed by the IDA Credit. All costs include contingencies

<sup>2/</sup> Includes goods to be procured through national shopping, consulting services, working capital for subprojects and operating costs.

**Table A1: Consultant Selection Arrangements (optional)**  
(US\$ million equivalent)

Consultant Services Expenditure Category	Selection Method							Total Cost <sup>1</sup>
	QCBS	QBS	SFB	LCS	CQ	Other	N.B.F.	
<b>A. Firms</b>	0.96 (0.96)	0.00 (0.00)	0.00 (0.00)	0.00 (0.00)	0.20 (0.20)	0.64 (0.64)	0.58 (0.00)	2.38 (1.80)
<b>B. Individuals</b>	0.00 (0.00)	0.00 (0.00)	0.00 (0.00)	0.00 (0.00)	0.54 (0.54)	0.00 (0.00)	0.00 (0.00)	0.54 (0.54)
<b>Total</b>	0.96 (0.96)	0.00 (0.00)	0.00 (0.00)	0.00 (0.00)	0.74 (0.74)	0.64 (0.64)	0.58 (0.00)	2.92 (2.34)

1) Including contingencies

Note: QCBS = Quality- and Cost-Based Selection

QBS = Quality-based Selection

SFB = Selection under a Fixed Budget

LCS = Least-Cost Selection

CQ = Selection Based on Consultants' Qualifications

Other = Selection of individual consultants (per Section V of Consultants Guidelines), Commercial Practices, etc.

N.B.F. = Not Bank-financed

Figures in parenthesis are the amounts to be financed by the Bank Credit.

**Prior review thresholds (Table B)**

IDA's prior review will be required for a) contracts with consulting firms above US\$100,000 and any sole-source contract; and b) contracts with individual consultants above US\$30,000. In addition to the prior review of individual procurement actions, an annual procurement plan and budget will be reviewed and approved by the Bank each year.

**Table B: Thresholds for Procurement Methods and Prior Review<sup>1</sup>**

<b>Expenditure Category</b>	<b>Contract Value Threshold (US\$ thousands)</b>	<b>Procurement Method</b>	<b>Contracts Subject to Prior Review (US\$ millions)</b>
<b>1. Works</b>	N/A	N/A	N/A
<b>2. Goods</b>	>25,000 < 25,000	NCB shopping	None None
<b>3. Services</b>			
<b>Consulting Firms (including subgrants)</b>	>100 <100	QCBS "	All (0.5 m.) Only TORs
<b>Individual Consultants</b>	>30,000 <30,000	Qualifications "	All (0.4 m.) Only TORs
<b>4. Goods and works under Complementary subproject grants</b>	N/A	commercial practices--shopping	None
<b>5. Recurrent costs</b>	N/A	N/A	N/A

**Total value of contracts subject to prior review: 1.35 m.**

**Overall Procurement Risk Assessment**

**Average**

**Frequency of procurement supervision missions proposed:** One every 12 months (includes special procurement supervision for post-review/audits)

<sup>1</sup>Thresholds generally differ by country and project. Consult OD 11.04 "Review of Procurement Documentation" and contact the Regional Procurement Adviser for guidance.

## **Disbursement**

### **Allocation of credit proceeds (Table C)**

The project will be disbursed over a three-year period. Disbursements will be made against the categories of expenditures indicated in Table C. The project is expected to be completed by June 30, 2004 and the Credit Closing Date would be December 31, 2004.

**Table C: Allocation of Credit Proceeds**

<b>Expenditure Category</b>	<b>Amount in US\$million</b>	<b>Financing Percentage</b>
1. Goods	0.06	100% foreign expenditures 85% local expenditures; unless UN agency, then 100%
2. Consultant Services	2.03	100%
3. Complementary Subprojects	5.04	100%
4. Training	0.07	100%
5. Unallocated	0.80	
<b>Total Project Costs</b>	<b>8.00</b>	
<b>Total</b>	<b>8.00</b>	

### **Special account:**

No Special Account will be established.

### **Financial Management:**

The results of the financial assessment indicates that although FAO-Honduras has a financial management system that meets their needs, this systems does not fully meet Bank requirements, and therefore cannot yet generate project management reports (PMRs). In addition, the staff for the Project Implementing Unit (UTA) who would be responsible for project management have not been hired yet. As a result, an action plan has been agreed with FAO-Honduras to achieve by project effectiveness the certification of the project's financial management system with PMR capabilities, as required under the Bank's Loan Administration Change Initiative (LACI). In the event that by project effectiveness FAO-Honduras has not fully implemented a financial management system with PMR capabilities, at least a system that meets minimum Bank requirements should be in place. FAO-Honduras will implement an adequate integrated financial management system for the project, including internal control systems that: (i) are in accordance with international accounting standards; (ii) reliably record and report all assets, liabilities and financial transactions of the project; (iii) provide sufficient financial information for managing and monitoring project activities; and (iv) integrates financial information, disbursements, purchasing, procurement, and control of contracts, to allow the generation of quarterly programmatic financial reports on the financial and physical advance of each component, as well as financial information by disbursement category. The detail of these procedures will be contained in the Operational Manual.

**Auditing Arrangements:**

An external auditor, acceptable to IDA, will be contracted by the FAO-Honduras to carry out an annual financial audit of the project, as required by OP/BP 10.02 by Credit Effectiveness. The auditor will be selected in accordance with the Bank's "Guidelines for the Selection and Employment of consultants by the World Bank Borrowers" dated January 1997, revised in September 1997. The auditors should be hired at project inception, and prior of the commencement of each project fiscal year thereafter, so that the interim audits can be performed throughout each year of project implementation. The project financial statements, SOEs and the PMRs (if applicable), will be audited at the end of each fiscal year during project implementation. An audited of the project financial statements will be submitted to the Bank within 180 days of the close of the project's financial year. The "Guidelines and Terms of Reference for Audits of Projects with Financing by the World Bank in the Latin American and the Caribbean Region" should be followed by the IHT when preparing the terms of reference for the audit and these guidelines should be provided to the selected auditors

**Disbursement Procedures:**

If by project effectiveness FAO-Honduras does not have in place a PMR compliant financial management system, but meets minimum Bank's financial management requirements, the traditional disbursement procedures will be used for withdrawal of funds under the credit agreement, in accordance with the guidelines set in the Disbursement Procedures Handbook. SOEs documentation will be maintained by FAO-Honduras for post-review and audit purposes. The authorized allocation(s) for the transfer of funds to FAO-Honduras will be set at a level sufficient to cover approximately six months of estimated expenditures eligible for financing by the Bank. Replenishments of funds will be made on evidence of satisfactory utilization of the previous advance(s) as evidenced by the documentation submitted in support of disbursement applications. Deposits into FAO project account and its replenishments, accompanied with the supporting and other documentation specified in the Disbursement Handbook. Withdrawal applications will be fully documented, except for expenditures under contracts costing less than US\$ 20,000 equivalent for goods, and US\$100,000 and US\$ 30,000 equivalent for consulting firms and individual consultants, respectively.

**Use of Project Management Report (PMRs):**

At FAO-Honduras requests, and upon implementation of a PMR compliant financial management system, transition to a full Project Management Report (PMR) system could be approved. The PMRs would serve as disbursement requests. Transition to PMR will be subject to the satisfactory results of new financial management and procurement assessments. Once FAO becomes PMR compliant, disbursements would be in accordance with guidelines set in the Loan Administration Change Initiative (LACI) Implementation Handbook. Each application for withdrawal should separately identify the funds requested from the credit Account, and would be supported by a Project Management Report (PMR) or such other documents and evidence as the Bank may request. PMRs should be submitted within 45 days from the preceding quarter. Upon receipt of each application for withdrawal, the Bank, on behalf of the Borrower, shall withdraw from the credit account and deposit into the Special Accounts an amount equal to the lesser: (a) the amount requested; and (b) the amount the Bank has determined, based on the PMR accompanying the application, is required to be deposited in order to finance eligible expenditures during the six month period following the date of the report, but in no case should exceed 20% of the total credit funds, without prior authorization from the Loan department. FAO-Honduras would be responsible for preparing withdrawal applications and the related PMRs. All supporting documentation authenticating the expenditures reported in the PMRs would be maintained by FAO-Honduras and made available for review

by independent auditors and by the Bank supervision missions. Direct Payments and Special Commitments should be clearly identified in the PMRs and FAO-Honduras shall include the documentation required for these types of payments.

**Transfer of Project Funds:**

Credit funds will be transferred at a designated bank account in US Dollars at FAO Headquarters, from where transfer of funds will be made to FAO-Honduras and maintained in a US Dollars and in a separate account at a commercial bank. FAO-Honduras, with INA's clearance and through the Ministry of Finance of Honduras, will be responsible for submitting appropriate disbursement applications to request the transfer of funds. Replenishments of funds under SOEs will be made on evidence of satisfactory utilization of the previous advance(s) as evidenced by the documentation submitted in support of disbursement applications. Initial transfer of funds and subsequent replenishments, up to the Authorized Allocations will be made initially on the basis of Applications for Withdrawals (Form 1903) accompanied with the supporting and other documentation specified in the Disbursement Handbook. Once FAO-Honduras, is PMR compliant, certified as such by the Bank, and FAO-Honduras requests transition to disbursements PMR based, any subsequent disbursement from the credit account would be to cover estimated eligible expenditures for the next six-months of cash forecast reported in the PMR, as described hereafter.

**Retroactive Financing.**

Retroactive financing may be made on account of payments made for the eligible expenditures from project negotiations (November 1, 2000) in an aggregate amount not exceeding SDR 31,000 (US\$ 40,000 equivalent).

**Annex 6, Table D : Financial Management Action Plan**

	<b>Action</b>	<b>Responsible</b>	<b>Estimated date of Conclusion</b>
1.	Definition of Project indicators for physical and financial monitoring	FAO – Carlos Zelaya	11/30/00
2.	Update of project operations manual and financial manual for the land purchases and complementary subprojects	FAO - Consultants	01/30/01
3.	Preparation of administrative procedures manual	FAO – UTA Financial Director	01/30/01
4.	Design and implementation of financial management system (FMS)	FAO- UTA and consultant	01/30/01
	(a) Consultant contracted	FAO – Carlos Zelaya	01/09/01
	(b) System designed	Consultant	03/30/01
	(c) System implemented	FAO – UTA and consultant	04/02/01
5.	Contracting of external auditors		
	(a) Short list and TORs submitted to the Bank	FAO – Carlos Zelaya	15/11/00
	(b) Auditors contracted	FAO – Carlos Zelaya	Effectiveness
6.	Design of temporary records and reports in excel, to be used until the FMS in action No. 5 above is implemented	FAO - Consultant	02/15/01
7.	Hiring of project Staff for the UTA		
	Project Director and Finance Director		
	(a) Advertising of position	FAO & INA	11/13/00
	(d) Contracting	FAO & INA	01/05/01
	Technical officers and administrative staff	FAO - UTA	03/31/01
8.	Preparation of annual project operating plan	FAO- UTA Project Director	01/02/01

**Annex 7: Project Processing Schedule**  
**HONDURAS: Access to Land Pilot Project (PACTA)**

<b>Project Schedule</b>	<b>Planned</b>	<b>Actual</b>
Time taken to prepare the project (months)	15	15
First Bank mission (identification)	02/15/99	02/15/99
Appraisal mission departure	05/08/2000	05/08/2000
Negotiations	10/17/2000	10/30/2000
Planned Date of Effectiveness	12/12/2000	

**Prepared by:**

Instituto de Reforma Agraria, Ministry of Agriculture and Livestock and the Project Coordination Unit,  
Rural Land Management Project (PAAR), Ministry of Agriculture and Livestock

**Preparation assistance:**

Carlos Zelaya, institutional framework (FAO-Honduras); Javier Molina (FAO-Santiago), land fund specialist; Fernando Soto (RUTA), financial assessment and regulatory framework; Ismalia Acosta, Legal Analysis; Carlos Barahona (University of Reading), Social Assessment; Santiago Diaz, eligibility of financial institutions; Lorena Deras, financial regulations.

**Bank staff who worked on the project included:**

<b>Name</b>	<b>Speciality</b>
Augusta Molnar	Task Manager, LCSES
Jeff Muller	Natural Resource Economist
James Smyle	Forestry Specialist, LCSES
Michael Goldberg	Financial and Micro Credit, LCRFP
Reynaldo Pastor	Sr. Counsel, LEGOP
Tom Korczowski	Land Administration Specialist, Consultant
Robin Mearns	Social Geographer, EASRD
Teresa Roncal	Procurement Analyst, LCSES
Juan Martinez	Social and Indigenous Specialist
Luz Zeron	Financial Management Specialist
Enzo de Laurentiis	Sr. Procurement Specialist, LCSES

**Annex 8: Documents in the Project File\***  
**HONDURAS: Access to Land Pilot Project (PACTA)**

**A. Project Implementation Plan**

Draft Operations Manual (Manual Operativo)

Financial Regulations

Agreement between FAO and the Government of Honduras (final draft).

**B. Bank Staff Assessments**

- Aide Memoire Appraisal Mission, May 8-19, 2000 (In Spanish)
- Financial feasibility analysis -- Pedro Olinto mayo, 1999 ( Back to Office Report-English )
- Presentacion marzo, 2000 "Primer Encuentro de Actores del Proyecto Piloto de Fondo de Tierras para Honduras" (.ppt) TK marzo, 2000 (In Spanish)

**C. Other**

- ANALISIS LEGAL DEL PROYECTO PILOTO FONDO DE TIERRAS EN EL MARCO DE LA LEGISLACION VIGENTE EN HONDURAS -- Ismalia Acosta, Consultant, Sept, 2000 (In Spanish)
- UTF - Javier Molina, FAO-Santiago, 2000 (in Spanish)
- TCP - Carlos Zelaya, FAO-Honduras, 2000 (in Spanish)
- Social Evaluation -- Carlos Barahona, University of Reading, et.al. May, 1999 (in spanish)
- Fondo de Tierras Proyecto Piloto de Reforma Agraria Negociada -- TK sep, 1999 (In Spanish)
- REGLAMENTO, ANEXO 1: ELEGIBILIDAD DE INSTITUCIONES FINANCIERAS -- INDICADORES Y METODOLOGIA PARA LA EVALUACIÓN DEL DESEMPEÑO FINANCIERO DE INSTITUCIONES FINANCIERAS. Fernando Soto, Santiago Diaz junio, 2000 (In Spanish)
- FINANCIAMIENTO PARA LA ADQUISICION Y EXPLOTACION DE TIERRAS. REGLAMENTO -- Fernando Soto mayo 2000 (In Spanish)
- FINANCIAMIENTO PARA LA ADQUISICION Y EXPLOTACION DE TIERRAS. REGLAMENTO ANEXO 2: PROCEDIMIENTOS PARA LA APLICACIÓN DEL REGLAMENTO FINANCIERO -- Lorena Deras, Fernando Soto julio, 2000 (In Spanish)
- Presentacion marzo, 2000 "Primer Encuentro de Actores del Proyecto Piloto de Fondo de Tierras para Honduras" (.ppt) TK marzo, 2000
- Acta de Constitucion de la PACTA, Reunion Inicial, September 7, 2000. (In Spanish)
- Rural INVEST Course Materials, RUTA, Costa Rica (in Spanish).
- **Acuerdo Presidencial 893-00 (Creador de PACTA) 27 junio 2000.**
- Ley de Modernizacion y Desarrollo del Sector Agricola (LMSDA), Decreto 31-92.

\*Including electronic files

**Annex 9: Statement of Loans and Credits**  
**HONDURAS: Access to Land Pilot Project (PACTA)**

Project ID	FY	Borrower	Purpose	Original Amount in US\$ Millions			Difference between expected and actual disbursements*		
				IBRD	IDA	Cancel.	Undisb.	Orig	Frm Rev'd
P007396	1995	Honduras	ENVIRON. DEVELOPMENT	0.00	10.80	0.00	1.19	1.68	1.73
P060785	2001	Honduras	HN ECONOMIC & FIN.MANAGEMENT PROJECT	0.00	19.00	0.00	18.56	0.00	0.00
P007399	1995	Honduras	HN/BASIC EDUCATION	0.00	30.00	0.00	5.55	8.03	0.00
P048651	1999	Honduras	HN/FHIS IV	0.00	67.50	0.00	23.78	-19.12	0.00
P007392	1993	Honduras	HN/NUTRITION/HEALTH	0.00	35.40	0.00	2.97	-7.91	2.66
P057350	1999	Honduras	PROFUTURO	0.00	8.30	0.00	7.05	1.09	0.00
P007387	1996	Honduras	PUB SEC MOD SAC	0.00	115.70	0.00	26.68	1.13	36.83
P007398	1997	Honduras	RURAL LAND MGMT	0.00	34.00	0.00	15.64	9.04	9.01
P007388	1993	Honduras	TRNSPRT SCTR RHB	0.00	85.00	0.00	8.63	-11.75	8.39
<b>Total:</b>				<b>0.00</b>	<b>405.70</b>	<b>0.00</b>	<b>110.05</b>	<b>-17.81</b>	<b>58.62</b>

**HONDURAS**  
**STATEMENT OF IFC's**  
**Held and Disbursed Portfolio**  
**20-Sep-2000**  
**In Millions US Dollars**

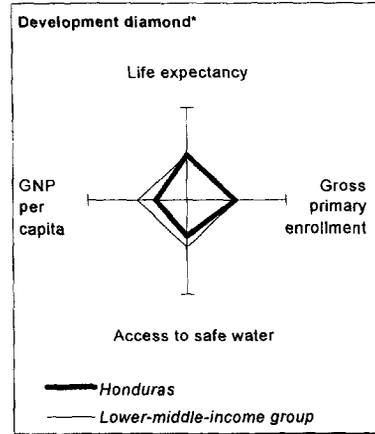
FY Approval	Company	Committed				Disbursed			
		IFC				IFC			
		Loan	Equity	Quasi	Partic	Loan	Equity	Quasi	Partic
1998	Camino Real Plaz	10.00	0.00	0.00	0.00	8.00	0.00	0.00	0.00
1995/98	Elcosa	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
1986/99	Granjas Marinas	6.00	0.00	0.00	0.00	6.00	0.00	0.00	0.00
	<b>Total Portfolio:</b>	<b>16.00</b>	<b>0.00</b>	<b>0.00</b>	<b>0.00</b>	<b>14.00</b>	<b>0.00</b>	<b>0.00</b>	<b>0.00</b>
		Approvals Pending Commitment							
FY Approval	Company	Loan	Equity	Quasi	Partic				
2000	Agopalma	7000.00	0.00	0.00	0.00				
1999	Celtel Honduras	5000.00	5000.00	0.00	15000.00				
	<b>Total Pending Commitment:</b>	<b>12000.00</b>	<b>5000.00</b>	<b>0.00</b>	<b>15000.00</b>				

## Annex 10: Country at a Glance

### HONDURAS: Access to Land Pilot Project (PACTA)

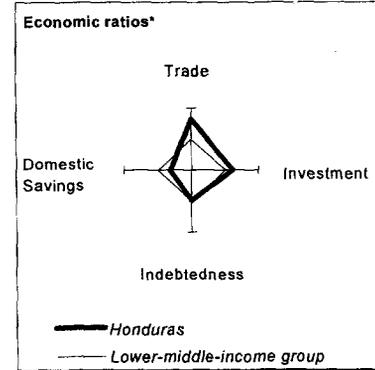
#### POVERTY and SOCIAL

	Honduras	Latin America & Carib.	Lower-middle-income
<b>1999</b>			
Population, mid-year (millions)	6.3	509	2,094
GNP per capita (Atlas method, US\$)	760	3,840	1,200
GNP (Atlas method, US\$ billions)	4.8	1,955	2,513
<b>Average annual growth, 1993-99</b>			
Population (%)	2.8	1.6	1.1
Labor force (%)	3.8	2.5	1.2
<b>Most recent estimate (latest year available, 1993-99)</b>			
Poverty (% of population below national poverty line)	53	..	..
Urban population (% of total population)	52	75	43
Life expectancy at birth (years)	69	70	69
Infant mortality (per 1,000 live births)	36	31	33
Child malnutrition (% of children under 5)	25	8	15
Access to improved water source (% of population)	65	75	86
Illiteracy (% of population age 15+)	26	12	16
Gross primary enrollment (% of school-age population)	111	113	114
Male	110	..	114
Female	112	..	116



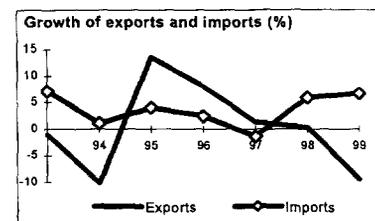
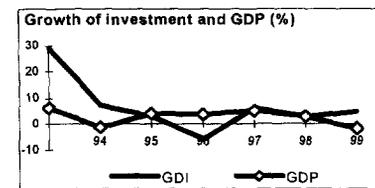
#### KEY ECONOMIC RATIOS and LONG-TERM TRENDS

	1979	1989	1998	1999	
GDP (US\$ billions)	2.3	5.2	5.2	5.4	
Gross domestic investment/GDP	26.8	19.1	30.8	32.9	
Exports of goods and services/GDP	36.6	29.0	47.2	42.9	
Gross domestic savings/GDP	22.0	13.7	24.6	19.1	
Gross national savings/GDP	18.0	9.9	25.3	22.9	
Current account balance/GDP	-8.8	-7.9	-5.5	-10.0	
Interest payments/GDP	2.7	0.9	3.5	3.2	
Total debt/GDP	52.6	65.5	95.3	99.4	
Total debt service/exports	20.5	12.6	18.2	13.4	
Present value of debt/GDP	..	..	61.4	..	
Present value of debt/exports	..	..	116.2	..	
<b>(average annual growth)</b>					
GDP	2.4	3.2	2.9	-1.9	5.3
GNP per capita	-0.7	0.8	0.4	-3.9	2.8
Exports of goods and services	0.5	1.5	0.3	-9.4	9.8



#### STRUCTURE of the ECONOMY

	1979	1989	1998	1999
<b>(% of GDP)</b>				
Agriculture	25.6	21.1	19.2	16.2
Industry	24.4	24.7	30.4	31.9
Manufacturing	15.1	15.0	18.6	19.6
Services	50.0	54.2	50.4	51.9
Private consumption	67.0	72.0	65.3	69.4
General government consumption	10.9	14.3	10.1	11.4
Imports of goods and services	41.4	34.4	53.3	56.7
<b>(average annual growth)</b>				
Agriculture	2.4	2.4	-2.9	-8.7
Industry	2.9	3.5	4.2	4.0
Manufacturing	3.0	3.8	3.4	2.6
Services	2.3	3.5	5.6	-0.2
Private consumption	2.8	3.0	3.4	0.8
General government consumption	3.9	-0.6	21.7	10.9
Gross domestic investment	0.0	8.0	2.8	4.7
Imports of goods and services	0.1	3.6	5.9	6.7
Gross national product	2.5	3.7	3.3	-1.3

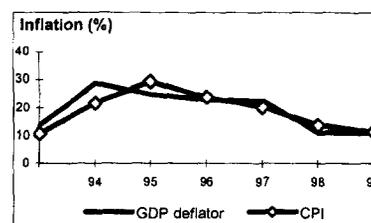


Note: 1999 data are preliminary estimates.

\* The diamonds show four key indicators in the country (in bold) compared with its income-group average. If data are missing, the diamond will be incomplete.

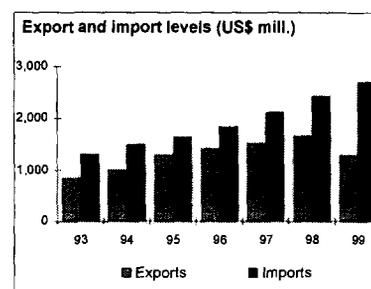
## PRICES and GOVERNMENT FINANCE

	1979	1989	1998	1999
<b>Domestic prices</b>				
<i>(% change)</i>				
Consumer prices	..	9.9	13.7	11.6
Implicit GDP deflator	11.5	7.1	11.0	11.1
<b>Government finance</b>				
<i>(% of GDP, includes current grants)</i>				
Current revenue	..	..	18.8	19.4
Current budget balance	..	..	4.1	2.8
Overall surplus/deficit	..	..	-1.7	-4.4



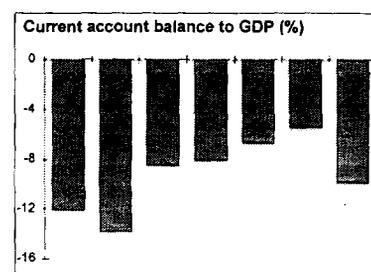
## TRADE

	1979	1989	1998	1999
<i>(US\$ millions)</i>				
Total exports (fob)	..	903	1,657	1,304
Bananas	..	352	176	38
Coffee	..	191	430	256
Manufactures	..	..	..	..
Total imports (cif)	..	1,045	2,445	2,718
Food	..	172	364	397
Fuel and energy	..	146	214	256
Capital goods	..	220	615	724
Export price index (1995=100)	..	98	94	90
Import price index (1995=100)	..	76	93	91
Terms of trade (1995=100)	..	129	102	99



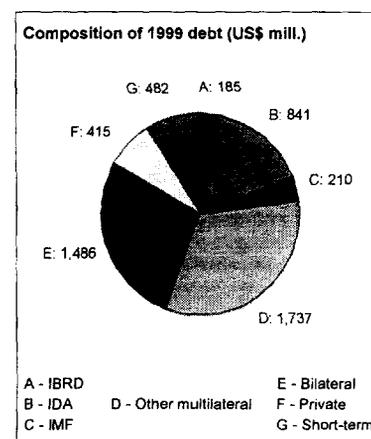
## BALANCE of PAYMENTS

	1979	1989	1998	1999
<i>(US\$ millions)</i>				
Exports of goods and services	838	1,061	2,476	2,312
Imports of goods and services	930	1,273	2,797	3,055
Resource balance	-92	-213	-322	-743
Net income	-120	-240	-209	-160
Net current transfers	14	43	241	365
Current account balance	-198	-410	-290	-538
Financing items (net)	218	364	458	880
Changes in net reserves	-20	45	-168	-342
<b>Memo:</b>				
Reserves including gold (US\$ millions)	..	28	770	1,209
Conversion rate (DEC, local/US\$)	2.0	2.0	13.4	14.2



## EXTERNAL DEBT and RESOURCE FLOWS

	1979	1989	1998	1999
<i>(US\$ millions)</i>				
Total debt outstanding and disbursed	1,184	3,386	5,002	5,356
IBRD	132	528	235	185
IDA	47	79	579	841
Total debt service	179	142	505	367
IBRD	14	1	68	65
IDA	1	0	6	7
Composition of net resource flows				
Official grants	21	71	163	210
Official creditors	86	86	19	158
Private creditors	63	43	109	-35
Foreign direct investment	28	51	84	222
Portfolio equity	0	0	..	..
World Bank program				
Commitments	35	0	59	61
Disbursements	32	2	64	273
Principal repayments	4	0	50	49
Net flows	29	2	14	224
Interest payments	11	1	24	22
Net transfers	17	1	-10	202



**Additional  
Annex No.: 11**

**Summary of the Social Assessment**

**Introduction**

A social assessment was performed using a participatory methodology in the areas proposed for the pilot phase of PACTA. The objectives of the assessment were to i) analyze the viability of the proposed implementation scheme in all its aspects; ii) help to define the roles of the respective actors in the process; iii) identify the needs of beneficiaries to participate effectively and to examine in particular the concept of a productive enterprise where individual ownership and choices have to be reconciled with need to take actions and decisions as a group; iv) make recommendations about an appropriate methodology for follow-up and evaluation in light of the demand-driven nature of the program and the decentralization of program administration and implementation, including design of a participatory monitoring and evaluation system.

Establishment of a "land fund" program has been a long standing demand of peasant organizations in Honduras and although this model differs from the original expectation that Government would create a separate, public fund for land purchase (as outlined in the LMSDA), there is now a broad-based acceptance in civil society of a complementary access to land model. This acceptance is the result of preparation work, including the social assessment, and the linked dialogue with civil society led by INA. This administration has been keen to advance on land tenure issues, and the President of Honduras has prioritized PACTA in the agenda of INA.

**Background on the Target Population**

As defined by the eligibility criteria of PACTA, the target population is very broad. These criteria, to be detailed in the Operations Manual, define a mixed class of landless agricultural workers (jornaleros and migratory workers), producers whose access to land is precarious (short term rentals, borrowers, or other informal access based on share-cropping or similar arrangements) or, if they have outright possession, then usually very small plots (< 1 ha.) of poor quality land.

The most recent agricultural census (1993) indicated that one out of four, or around 80,000 producers, were confined to less than 1 ha. of land. (In the 1950s one out of 10 producers had less than 1 hectare.) This was the fastest growing segment of producers in the 20 year period between the census of 1974 and 1993. Prior to the LMDSA, *minifundio* was defined as plots of less than 5 has. The census data show that more than seven out of ten producers have less than this amount of land.

There is no indication to believe that the same trend to the increasing fragmentation of family scale holdings is not still in effect; and that the overall pattern of landholding has not continued to grow ever more skewed. On a regional basis, increasing land pressure in the western part of the country coupled with the difficulties in implementing of the agrarian reform (which peaked in the mid-1970s) has also contributed to the increased colonization of remaining forest reserves. The same process has led to increased incidence of conflict with indigenous communities. The vast majority of the increase in land in farms that occurred in the inter-census period is located in the departments of Colón and Olancho, precisely the areas most clearly identified as 'frontier' zones. The agrarian reform of the 1970s also contributed to this process since it was largely a colonization program on national lands with the largest single project devoted to development of the Aguán Valley in Colón. Now these same lands, once converted under government auspices into agrarian reform cooperatives, have in large part been sold off to agro-export companies and others.

In addition to the rapidly growing rural population with very limited and precarious access to land, there is a vastly increasing number of landless peasants not detected by the census data. Estimates vary, but a reasonable guess would place the total number of families with no access to land (excluding workers on the agro-export plantations), or with less than 1 hectare, at around 50 per cent of the rural population of Honduras.

Within the very large pool of families potentially eligible for participation in PACTA, the respective UTLs would have to establish priorities and identify a fairly small client base with which to work given the limited resources of the pilot project. The UTLs have established the presence, working relationships and legitimacy within their respective areas of influence to undertake this process in a fair manner. Initial efforts will focus on eligible families with some prior organizational experience.

#### **Lack of access to land and credit market.**

The concentration of the best lands among a small percentage of landholders (less than 4% of farms have more than 50% of total land) makes it extremely difficult for family scale producers to participate effectively in the land market. Private land is available in the formal and informal land markets, but is seldom available to the smallest producers, since they do not have the needed collateral and cannot bid on the larger size productive plots that more often enter the market. PACTA is therefore designed to provide an economy of scale to producers who wish to purchase land. Such transfers would be likely to result in more intensive use. While individuals can also be beneficiaries, the majority of the participants are expected to be groups of producers who collectively identify land for sale, develop a business plan for that land, and assume collective responsibility for investment and repayment until the loan is paid off, and they can exercise their individual rights over their own parcels. Some groups may select a production model that entails long-term cooperative investment. Most are expected to parcel the land and farm as individuals.

Although informal credit providers have multiplied and in some cases achieved great success, these organizations are far too undercapitalized and lack adequate controls to enable either land purchase or substantial improvements. Credit of this sort is at best useful for short-term consumption needs and working capital; and tends to be available only at very high interest rates.

#### **Social Assessment**

The social assessment included consultations in sample regions where the program will be carried out. The main public demands for land access have been made by the main peasant organizations in the context of FONTIER and linked to the demands of the cooperatives created in the land reform period. There was initially a resistance to the PACTA because it did not address these particular issues. Over the course of preparation, however, this resistance has disappeared and some of the same political actors have agreed to sit on the advisory board of PACTA. The social assessment found that interest in the model is more widespread, and rural producers who are not members of the main peasant associations are also expressing strong interest in participating in the model.

The social assessment indicates that there is a strong demand for PACTA. The main issues addressed in design are:

**Individual ownership and the enterprise.** An underlying principle of the PACTA model is that risks of failure can only be controlled in a demand-driven scenario that does not impose farm models or forms of association that are not of interest to the participants. The form of association, property regime (individual

or group), and system of production implemented by its members will be self-determined. The basic criterion for establishing an enterprise to be financed is that it be legally constituted as such to enter into credit contracts and purchase-sale agreements.

A legal analysis has been conducted to outline the options available under Honduran law for groups to acquire property and assure property rights to each member. The options available – and the internal regulations adopted by each group – would determine how property rights are assigned within the enterprise; how responsibility for loan repayment is managed; whether or not collective areas are established initially; and so on. An explanation of the options and the procedures to implement each one will be incorporated in the operations manual.

The social assessment showed clearly that legal services and organizational support will be equally important as technical services related to production and commercialization. In general, the social assessment confirmed that the most viable scenario will be to deliver services and arrange for credit with groups of 8 to 20 families while the same groups will decide to sub-divide most of the acquired land. The experience of PILARH has been that some groups have initiated collective areas of production, made group purchases, etc. once having established a minimum degree of stability. A broad range of models is expected.

#### **Representative case studies of beneficiaries.**

The case studies summarized in the Social Assessment describe i) groups of probable future participants in PACTA from different regions and ii) groups who have been organized in PILARH. (See D2) In the case of PILARH, the case study shows the group formed entirely of landless farm workers; gradual but consistent diversification of production; significant employment generation with a group of 11 being able to hire 20 temporary workers during peak periods in the 4th year; excellent credit performance; capacity to make additional fixed investments after the first few years; greatly enhanced food security; more intensive use of family labor; and evidence of greater social and familial stability with a reduction in alcoholism and greater participation in the wider community.

A case study in Comayagua of a group likely to participate in PACTA consists of 8 women who have established a Caja Rural; received training in financial management from one of the prospective UTL; and produced high value crops on 5 has. of rented, irrigable land. The group has prepared a plan for land purchase but lacks financing. This group has evident strengths to build upon in administration and production but confronts risks related to commercialization. Indeed, this latter problem was encountered in every area.

The Social Assessment recommended that the future UTA sponsor training for the UTLs on market access; and that successful experiences – such as that of PRODELICAS in Colón – should be ‘socialized’ by means of a program to share best practices among the different service providers.

In summary, regarding group size and composition, the groups likely to participate in PACTA would have between 8 to 20 members; be experienced in agriculture; and may have participated in other aspects of a local rural development program as in the example of the Caja Rural or programs focused on appropriate technology. Other participants would include producers decapitalized as a result of Mitch, campesino organizations without land, participants in local development organizations, or as in the case of PILARH groups that start from scratch for the express purpose of acquiring land. The groups must be willing to formally accept training related to enterprise formation. Members should reside in the same vicinity where the sub-project is to be established.

### **Women's participation**

The role of women in rural development projects in these areas is increasingly important. Enabling women's participation is important to the most basic project goals of poverty reduction.

Some of the UTLs have a gender component and have hired women in positions of authority (such as the director of PILARH). More than 50 percent of the Cajas Rurales in Comayagua are managed by women. The social assessment found that many groups of women already formed for different purposes are likely to be candidates for land purchase.

Reflecting a widespread opinion, in the Social Assessment noted that: "women's skills as administrators, high level of responsibility with respect to obligations, and seriousness in their work [as participants in rural development projects] indicate that women will play an important role in PACTA." The UTA will monitor the level of participation of women in the process and promote the rights of women (especially property rights) as full members of all groups acquiring land.

### **Targeting eligible families.**

The programs run by the UTLs are almost entirely rooted in working with the population eligible for participation in PACTA. The draft operations manual suggests that the UTLs work with known members of the local community and that proof of eligibility where it is not self-evident should rely upon the verification of the municipality, church, or other local organization, including the CLA.

### **Participatory Monitoring and Evaluation.**

Given the pilot nature of PACTA, it is very important to generate adequate information to evaluate the viability of the program and to make the needed adjustments before considering launching the program on a broad scale. The social assessment established the framework for a participatory monitoring and evaluation (PM&E) system, and generated case study information that can serve as a baseline for the program. The PM&E will be linked to the on-going monitoring system used by the PILARH land program, so that comparisons can be made with PACTA areas and beneficiaries from that earlier pilot operation. While preliminary indicators were identified during the social assessment, the final indicators for measure will be selected by stakeholders once the program is initiated.

The PM&E will concentrate on the following types of information:

1. operative processes of the pilot project
2. social and economic impact of the pilot project; and
3. institutional learning within PACTA to facilitate improvement of the pilot project during implementation.

The system of PME will involve all of the actors, in each of the main activities of PACTA, in the definition of objectives, indicators, methods and uses of the information generated in the process. The system will facilitate the participation of those actors who otherwise might not be able to express their point of view and influence the development of the project through the traditional methods of project monitoring, in particular the campesino families who participate in PACTA. The system will be based upon participatory methods and efficient information management to enable the project to systematize the experiences gained in each region and to facilitate institutional and social learning processes.

Given the innovative nature of the pilot project it is important to establish a system that involves the principal actors from the very beginning. This will permit discussion and agreement between these actors

about the objectives, indicators, methods of measurement, calendar of activities, report writing, creation of feedback mechanisms and the progressive modification of procedures. The system for PM&E should create the conditions and means for all actors to play an active role in the evolution of the pilot project.

### **Design of PM&E in the pilot project.**

Given the decentralized structure of PACTA, three sub-systems for PM&E are proposed, each one of which should generate insights on the three points mentioned above.

**Sub-system 1:** On the decentralized implementation; the relations between the UTA and the UTLs.

**Sub-system 2:** On the implementation of PACTA in each region; the relation between the UTLs, the productive enterprises formed in the framework of the project, and the Local Support Committees.

**Sub-system 3:** On the participation of the financial institutions; the relation between the UTA and the respective financial institutions that agree to take part in PACTA.

To establish these sub-systems the UTA will contract a team of consultants who are able to accomplish the following tasks:

- train the UTA and UTLs on PM&E;
- facilitate establishment of the 3 sub-systems mentioned above;
- carry-out periodic evaluations of the process of PM&E; and
- help to systematize the lessons learned and facilitate an institutional and social learning process that includes the different actors, including the GOH (principally INA) UTA, financial institutions, UTLs and the enterprises themselves.

The need to implement this activity within the framework of PACTA has been amply discussed during project preparation; and its importance in enabling a process of institutional and social learning is broadly recognized as key to the success of the pilot project.

**Institutional and social learning.** To derive lessons from the pilot project and to assure appropriation of the lessons on the part of the respective actors it is important to take a deliberate and systematic approach. The three sub-systems of PM&E are intended to enable PACTA to incorporate the respective actors in the following institutional and social learning processes:

1. An attempt will be made to systematically derive lessons through critical reflection on the decentralized implementation structure that should support further development of the model on a larger scale. That is to say, on a larger geographic scale by incorporating additional service providers established in a local context and by permitting UTLs involved in the pilot project to expand their scope of operations into new areas. The UTA will seek to develop the appropriate administrative model to apply in this framework; and assure that the lessons of the program are fully taken-up by the relevant institutions and in particular by INA. (Other national programs in Honduras that rely upon a similarly decentralized operational structure include PRONADERS and the Upland Fund.) From the perspective of the UTLs, PACTA both provides a forum and supports a set of practical measures that would enable a pluralistic group of actors in rural development to contribute to the formation of national agrarian policy. In this way, INA, the institution mainly responsible for agrarian policy, would be placed into a dynamic relationship with a new set of actors and indirectly into a relationship with a part of the campesino population that is outside the membership of organizations with roots in the agrarian reform of the 1970s. Finally, by establishing an approach to land policy that is integrated into the framework of local initiatives and priorities the entire process should become more sustainable. The approach being tested in PACTA has the advantage in this sense of being implemented in connection with rational land use, training, legal services, and credit arrangements that were typically absent in traditional approaches.

2. This strategy will also support local capacity building by strengthening the UTLs as service providers with a broader product offering. In the experience of PILARH, the capacity to provide a broad range of services consistently over time was clearly key to the success of the program. In addition, by working with local support committees (CLA) the UTLs will improve the level of transparency and participation of civil society. The UTA will promote the regular exchange of experiences between regions so that the UTLs can learn from each other. The groups formed in the framework of PACTA will be supported to develop a set of capabilities through the process of formulating a plan, establishing their own enterprise, negotiating land purchase and credit agreements, and in management training. Here it is appropriate to speak of a social learning process whereby the participants in PACTA are not only able to obtain a significant patrimony in land but become linked with the formal credit system and trained in a range of management and organizational skills that enable them to achieve fully autonomous operation. The benefits of this process in the rural communities where the enterprises are formed should be substantial.

3. In relation to the involvement of private credit institutions PACTA will (i) facilitate permanent links between the financial institutions and small scale producers by helping the former to identify new, viable markets and credit products; and (ii) will actively seek to promote adoption of appropriate credit technology in the process of serving this market. During project preparation, for example, several financial institutions participated alongside credit specialists from the UTLs in a week long course on rural investment projects sponsored by RUTA. The participants obtained a common set of analytical tools to evaluate farm enterprises. In addition, the credit program run by PILARH has been recognized as a well founded model that could be transmitted by means of similar courses in the context of PACTA. In this way, the larger financial institutions will be able to address the needs of small scale producers in an efficient way.

**Additional  
Annex No.: 12**

**Financial Regulation and Institutional Arrangements**

This annex includes the relevant content of the draft regulations (financial and procedural) which govern PACTA, both institutional roles and the rules governing the financial scheme.

**Organization and Function**

By working through existing agencies experienced in rural development as implementing partners, the project can establish a decentralized and participatory approach. Project actors include: poor rural families, the State through the National Agrarian Institute (INA), local technical units (UTLs), private financial institutions and local support committees (CLA) which help to mediate the program on a community level.

In terms of the organizational structure, each entity has explicit operational roles defined in the project operations manual. Project entities include: the Board of Directors, the National Administrative Unit (UTA), the UTLs, other technical service providers, the groups of rural households who participate in the project and the CLA. Their functions are:

***Board of Directors -***

*Composition.* Established by governmental decree and composed by two government representatives, the Director of the UTA (who will not have a vote), two representatives of the UTL, two representatives of the financial institutions and three representatives from the principal producer organizations..

*Functions.*

- Define and establish program policies, regulations and procedures. Approve the Operating Plan and Budget.
- Select the Director of the UTA.
- Support the UTA in the activities related to the project's implementation.
- Follow-up to the project's execution.
- Resolve controversies that might arise during project execution.
- Review and approve any budget amendment that might affect the achievement of objectives and central activities of the project.
- Coordinate with other institutions, organizations, programs and projects with activities related to PACTA

***UTA -***

*Composition.* The UTA will facilitate and coordinate project implementation. The team will include: a Director, a financial supervisor, an operations supervisor and a coordinator for monitoring and evaluation of the project. This team will be supported by a secretary, an accountant and a messenger/clerk.

*Functions.*

- Carry out the project, assuring that policies and procedures are followed.
- Select, contract and supervise that UTLs that will provide technical and legal services to project participants.
- Support and follow-up the UTLs through training, interchange between the UTL, and legal advice and technical services related to production.
- Organize and help to carry out monitoring and evaluation activities for the project, particularly

Participatory Monitoring and Evaluation (Seguimiento y Evaluación Participativa-SEP).  
Carry out the project's financial management according to budget.  
Provide logistical support for successful implementation.

***Local Technical Units (UTLs) -***

*Composition.* They will be the entities in charge of project implementation in local areas and will be hired by the project's UTA. The Terms of Reference for the UTLs will be defined in the Operational Manual but in general the UTLs must be established organizations with proven experience with small farmers. The contracts will be fixed-term, and duration will be determined by the UTA, and they can be renewed after a performance evaluation of the UTL. During the pilot project a follow-up and evaluation mechanism will be established in order to determine if this approach to project implementation will be viable for a future stage of PACTA.

*Functions.*

Promote PACTA.

Identify and pre-select eligible land buyers, in accord with established program criteria .

Facilitate formation of land buyers' groups when considered appropriate for the formation of productive enterprises.

Develop human capital of the productive future enterprise, particularly in entrepreneurial management areas, credit management and legal aspects related to land acquisition.

Participate in follow-up and the participatory monitoring and evaluation process of the project, including evaluation of services rendered by UTLs.

Support land buyers with relevant information about the land market and in legal analysis of the properties offered for sale.

Make sure buyers understand clearly the responsibilities of participating in the project, in particular with the financial institution and the consequences of defaulting on the loan for land.

Property valuation.

Support participants in defining the productive enterprise to be established in the property.

Support participants in preparing the request for bank credit.

Establish a list of eligible private service providers and evaluate their performance.

Inform the UTA periodically of UTL activities.

***Local Support Committee (CLA) -***

The CLA are existing community organizations that will advise and facilitate the work of the UTL in each area where the project is to be executed. The UTL must identify and select the contact person in a determined CLA, according to the conditions of each community.

*Functions.*

Advise and support UTL on a voluntary basis in the promotion of PACTA in the community.

Support UTL in the pre-selection of potential buyers to make sure that this process is conducted fairly and in accord with the criteria and procedures established by PACTA.

Operate as an advisory organization that contributes to the working relationship among buyers and UTL. In cases of conflict it will support finding a local solution through peaceful negotiations.

***Service suppliers (PS) -*** These are companies or individuals that offer technical services that UTLs do not have the capacity to offer or that they decide to subcontract to optimize resources.

It is expected that in the medium term, productive enterprises will acquire services based on the available market. With that in mind, the UTL will prepare a list of service providers for public bidding, which will allow productive enterprises to choose based on current needs, price and quality.

**Private financial institutions (FIs).** A set of indicators and a methodology have been established to determine the eligibility of financial institutions that wish to participate in PACTA. [See “Elegibilidad de Instituciones Financieras: Indicadores y Metodología para la Evaluación Del Desempeño Financiero de Instituciones Financieras.” in the Project File for a complete description.] The FIs potentially eligible to participate will be: commercial private banks, financial cooperatives (savings, credit, et al.) and private development organizations. Financial institutions (FI) will be evaluated prior to becoming a participant in PACTA and once a year thereafter to assure continued compliance with eligibility guidelines. PACTA reserves the right to adjust the eligibility criteria as appropriate.

The indicators to be applied include the following:

- Loan portfolio quality (measure of potentially unrecoverable loans)
- Profitability
- Operating efficiency
- Capital adequacy

These four measures are used in a point system to determine the minimum qualifying score for any FI to participate. Four additional points are also evaluated:

Strategic plan of the institution  
Audited financial statements (transparency of operations)  
Credit and policy guidelines (knowledge and experience in credit management)  
Training and development program (to develop the institution)

Whenever available, the institution should provide audited information. However, given that most of the FI that might participate are not regulated and use different criteria to recognize risk, certain adjustments will have to be made to their financial statements. These adjustments are described in detail in Appendix 2 of the above mentioned document.

#### ***Financial Regulation governing the activities of PACTA***

Financial regulations have been prepared for PACTA and their approval by IDA are a condition of Credit effectiveness. The main contents are summarized here.

#### **Objectives.**

- 1) Producers receive financing that combines loan funds and grants for land acquisition and development of a sustainable farm-based enterprise.
- 2) The **loans** for land acquisition and possible farm investments and working capital will be provided by Financial Institutions (FI) out of their own resources. The FI will assume the risks related to the portion of loan that is for land purchase. The **grants** will be provided directly by INA with credit proceeds and will be used to complete the financing for working capital and complementary investments that are needed to establish a productive enterprise on the newly acquired land.
- 3) In addition to providing the means to take advantage of immediate opportunities to establish viable, farm-based enterprises, the financing should be structured in such a way that it provides incentives to the producers to achieve long term profitability and to the Financial Institutions to provide financing as needed.

In particular, this would mean:

- a) That the financial institutions learn to manage the risks involved in marketing intermediate and long term credit, including credit for agricultural activities, and that the credit market in rural areas would be broadened in the future.
  - b) That the producers perceive incentives to repay their debts and to become long term clients of the financial institutions.
  - c) That the local technical agencies (UTLs) that offer professional services (technical assistance, legal advice, project preparation, etc.) are motivated to enable their clients to obtain a loan and to improve their capacity and will to honor the financial obligations they acquire.
- 4) *Eligibility requirements applicable to the Financial Institutions interested in participating in PACTA have been established. [See documents on file]*

**About the Financing:**

- 5) Producers will obtain financing in two parts:
  - a) A **loan**, provided by the financial institution, primarily to finance land purchase.
  - b) A **grant** provided by PACTA, that will enable producers to make complementary investments that are indispensable for establishing a sustainable enterprise and generating sufficient additional income to repay the loan for land purchase.
- 6) These two components will be provided to the borrowers in a coordinated fashion so that it becomes possible to leverage loan funds from a FI; and to build-in incentives that encourage borrowers to repay. The proportion of each component in the total financing will be determined by the following criteria:
- 7) (a) the characteristics of the productive project and the overall capacity of the borrowers to repay; and (b) the maximum allowable amount of the grant established by PACTA.

**About the loans:**

- 8) The loans will be used to finance the entire cost of land purchase; and in some cases the loan amount may be increased to cover part of the cost of additional investments.
- 9) The loans will be funded by private financial institutions who will assume the risks involved in the credit operation. The FI will make independent decisions about credit applications based on market criteria.
- 10) The viability and size of the loans will depend mainly on the current and estimated future repayment capacity of the participating families. In addition to the productive project being proposed, repayment capacity will be determined through interviews and surveys used to establish current and projected cash flows.
- 11) The terms of the loan will be as follows:
  - a) **Amount to finance:** will be open ended; to be determined by the FI as a function of the repayment capacity of the borrower
  - b) **Interest rate:** market rate of interest; to be established by the FI that authorizes the credit

- c) **Loan period:** between 6 to 10 years; will be determined as a function of the income projections of the productive projects to be financed
  - d) **Amortization:** payments will be made at least annually (principal and interest). In case a grace period is needed it should be as short as possible and should require repayment of the interest portion of the loan during the grace period. The program will seek to establish incentives that encourage financial discipline and willingness to pay by the borrower.
  - e) **Guarantees:**  
Land will be used to guarantee the loan for land purchase. However, the FI may require additional guarantees against the potential default on the credit it provides, in particular in those cases where the loan includes funds for complementary investments in fixed or working capital not covered by the grant. GOH will apply an existing guarantee fund (e.g. the FONGAC guarantee fund managed by FONAPROVI), or implement a new guarantee fund to support such cases.
  - f) **Loan agreement:** There will be a formal loan contract between FI and the producers.
- 12) The structure of the loan will also be determined by the following criteria:
- a) **Sources of repayment.** The producers should be able to amortize the loan for land purchase exclusively by means of the income generated by the productive project or other income derived from the families' activities [e.g., off farm employment].
  - b) **Operating procedures of the FI:** The FI will adapt the loan, in addition, to its internal operating procedures and management practices: traditional banking or micro-finance. The use of one or the other of these approaches will enable the FI to accept and estimate the value of additional guarantees (product or fiduciary) and apply an individual or group credit methodology.

**About the grants:**

- 13) The direct grants to participants are indispensable to provide working capital and enable fixed investments to be made on the acquired land and thereby raise productivity; and should be disbursed in such a way that they provide incentives to achieve a good repayment record on the loans.
- a) The grants will provide an important incentive for the FI to provide loans for land because the grants would make it possible to execute a viable business plan on the acquired property.
  - b) Seventy per cent (70%) of the grant will be used to finance working and fixed capital investments during the first three years following land purchase.
  - c) The remainder of the grant (30%) will be used to reward participants for establishing very good repayment behavior and to further enhance productive capacity.
- 14) The amount of the grant to any participant (individual or group) cannot surpass, in any case, 45% of the total value of the investment in land, fixed capital and working capital, with a ceiling of \$3,500 per family.
- 16) Assignment of the grant will be on the following conditions:
- a) The recipients are clearly eligible for participation in PACTA
  - b) A sub-loan has been approved by one of the FI participating in PACTA and the producer has acquired title to the land purchased. In case a UTL acts as the lending agency the loan will not trigger assignment of a complementary grant.

- 17) The use of the grant will be conditioned in the following ways:
- a) The beneficiary must keep current on repayment of the loan for land purchase.
  - b) The grant may not be used to amortize the loan for land.
  - c) The grant will be released over three years according to the requirements of the business plan.

**Disbursement of grants to producers:**

- 20) Once the FI has authorized a loan for land on behalf of producers, the grant will be disbursed in two parts:
- (a) Of the total grant, 70% will be deposited in the producers' account and disbursed over the first three years based on the requirements of the business plan; and
  - (b) Thirty percent of the total grant will be transferred in the form of a three year or four year Certificate of Deposit (CD) (depending on whether or not a one year grace period is included in the loan terms).
- 22) The producers' account and the CD should be deposited in the same FI that makes the loan for land, on the condition that it is legally authorized to accept deposits and, preferably, is supervised by the *Comisión Nacional de Banca y Finanzas*.

**The Producers' Account:**

- 23) 70% of the total grant to any producer will be deposited in the producer's account.
- 24) The producers' account will have the following characteristics:
- a) The account will be in the name of the producers and the UTA.
  - b) The interest rate paid on the account will be the same as the FI ordinarily pays on the same type of account, in accord with the amount on deposit. The interest earned will be capitalized periodically.
- 25) The funds deposited in the account will be blocked except at those times and in those amounts defined elsewhere in these regulations. Use of the funds is conditioned on the specific actions of the business plan and requires the authorization of the UTA.
- 26) The producers may only use the grant funds deposited in the account in accord with a previously agreed upon business plan. However, use of the funds may be accelerated if the business plan does not work according to expectations. In this case, a new version of the business plan would be prepared and approved to justify a different withdrawal of grant funds.

**The Certificate of Deposit.**

- 27) The Certificate of Deposit represents the remaining balance of the grant. The participant may withdraw these funds on the date of maturity of the CD if a very good repayment behavior with respect to the land loan has been established. That is to say, if the producers have operated as good faith borrowers.
- 28) The CD will have the following characteristics:
- a) **Title.** The CD will have the same legal structure as the producers' account. The UTA will have a

registered signature on file, without which the participant cannot redeem the CD, and until all the requirements for its use have been fulfilled.

- b) **Term.** The CD will have a term of 3 years.
- c) **Interest Rate.** The CD will earn the same rate of interest as is normally paid by the FI for the same type of account, in accord with the amount on deposit. The interest earned will be capitalized periodically.

29) To redeem the entire amount of the CD on the date of maturity the participants must be in good standing with the FI that made the loan for land purchase.

31) In case a producer has fallen into arrears on loan repayment, consideration will be given to the causes to avoid unjustly penalizing producers operating in good faith. If the arrears are judged to have been due to causes not attributable to the producers, the CD will still be released, although adjustments to the business plan will have to be made. The evaluation of each such case will be made by personnel of the FI responsible for follow-up on the loan. If the producers disagree with the evaluation made by the FI, they will have recourse to an independent evaluation by PACTA. In the context of the pilot project, it is especially important to evaluate such cases. The evaluation by PACTA will include an analysis of the original business plan and the technical advice offered by the UTL. If the CD is not released to the producers, it will be returned to the UTA.

32) In those cases where participants are in good standing, the CD will provide the means to make new investments in the productive enterprise at a time when the participants are likely to be better prepared than they were at the very outset to manage the process of diversification. At this time, after having demonstrated the capacity and will to repay the loan for land, and having honored a substantial portion of the total debt, the producers will be in a good position to negotiate renewed financing, likely with the same FI which authorized the loan for land, for further investment in the enterprise.

#### **Executing the guarantee:**

33) When the borrower has failed to repay the loan for land and any investments without reasonable cause, the FI may proceed to execute the guarantee represented by the land, upon having fulfilled certain prior conditions (and, subsequently to make additional claims against the guarantee fund established by the GOH):

- a) The guarantee may not be executed for a period of 90 days after the borrower has failed to make two consecutive payments (measured from the due date of the second payment), including the interest only payment during the one year grace period.
- b) The justification for the late payments will have to be judged by the FI in accord with its own criteria and procedures;
- c) The FI must demonstrate that it has followed all the procedures for collection in accord with its own regulations (reminder letters, visits, etc.);
- d) The FI must have demonstrated that it has initiated the judicial process to execute the guarantee on the land.

### **Eligibility of financial institutions for participation in PACTA (Summary)**

A set of indicators and a methodology have been established to determine the eligibility of financial institutions that wish to participate in PACTA. [See “Elegibilidad de Instituciones Financieras: Indicadores y Metodología para la Evaluación Del Desempeño Financiero de Instituciones Financieras.” in the Project File for a complete description.] Financial institutions (FI) will be evaluated prior to becoming a participant in PACTA and once a year thereafter to assure continued compliance with eligibility guidelines.

The indicators to be applied include the following:

- Loan portfolio quality (measure of potentially unrecoverable loans)
- Profitability
- Operating efficiency
- Capital adequacy

These four measures are used in a point system to determine the minimum qualifying score for any FI to participate. Four additional points are also evaluated:

- Strategic plan of the institution
- Audited financial statements (transparency of operations)
- Credit and policy guidelines (knowledge and experience in credit management)
- Training and development program (to develop the institution)

Whenever available, the institution should provide audited information. However, given that most of the FI that might participate are not regulated and use different criteria to recognize risk, certain adjustments will have to be made to their financial statements. These adjustments are described in detail in Appendix 2 of the above mentioned document.

#### **Other types of financial institutions.**

There are two types of FI that are not regulated by the *Comisión Nacional de Banca y Finanzas*, including Private Development Organizations (OPD) and Credit and Savings Cooperatives (CAC). Some of these institutions may qualify for participation in PACTA by applying certain adjustments to their financial statements as described in the Eligibility Requirements.

- a) If a Private Development Organizations (OPD), not authorized by law to accept deposits, participates as a lender in PACTA then the savings account and CD will be placed in a FI that is so authorized.
- b) The Credit and Savings Cooperatives (CAC) are authorized by law to accept deposits only from their members. Project funds may not be used to pay membership fees.

