

CONFORMED COPY

CREDIT NUMBER 3549 MOZ

Development Credit Agreement

(Municipal Development Project)

between

REPUBLIC OF MOZAMBIQUE

and

INTERNATIONAL DEVELOPMENT ASSOCIATION

Dated August 15, 2001

CREDIT NUMBER 3549 MOZ

DEVELOPMENT CREDIT AGREEMENT

AGREEMENT, dated August 15, 2001, between REPUBLIC OF MOZAMBIQUE (the Borrower) and INTERNATIONAL DEVELOPMENT ASSOCIATION (the Association).

WHEREAS (A) the Borrower, having satisfied itself as to the feasibility and priority of the Project described in Schedule 2 to this Agreement, has requested the Association to assist in the financing of the Project;

(B) by an agreement dated April 2, 2001, between the Borrower and the Nordic Development Fund (the NDF Credit Agreement), the Nordic Development Fund has agreed to make a credit to the Borrower in a principal amount of SDR 4,000,000 (the NDF Credit) to assist in financing Part D of the Project on the terms and conditions set forth in the NDF Credit Agreement; and

WHEREAS the Association has agreed, on the basis, inter alia, of the foregoing, to extend the Credit to the Borrower upon the terms and conditions set forth in this Agreement;

NOW THEREFORE the parties hereto hereby agree as follows:

ARTICLE I

General Conditions; Definitions

Section 1.01. The "General Conditions Applicable to Development Credit Agreements" of the Association, dated January 1, 1985 (as amended through October 6, 1999), with the modifications set forth below (the General Conditions) constitute an integral part of this Agreement:

(a) A new paragraph (12) is added to Section 2.01 to read as set forth below, and the existing paragraphs (12) through (14) of said Section are accordingly renumbered as paragraphs (13) through (15):

"12. 'Participating Country' means any country that the Association determines meets the requirements set forth in Section 11 of Resolution No. 194 of the Board of Governors of the Association, adopted on April 8, 1999; and 'Participating Countries' means, collectively, all such countries." ;

- (b) The second sentence of Section 5.01 is modified to read:

“Except as the Borrower and the Association shall otherwise agree, no withdrawals shall be made: (a) on account of expenditures in the territories of any country which is not a Participating Country or for goods produced in, or services supplied from, such territories; or (b) for the purpose of any payment to persons or entities, or for any import of goods, if such payment or import, to the knowledge of the Association, is prohibited by a decision of the United Nations Security Council taken under Chapter VII of the Charter of the United Nations.”

Section 1.02. Unless the context otherwise requires, the several terms defined in the General Conditions have the respective meanings therein set forth and the following additional terms have the following meanings:

- (a) “Annual MG Investment Plan” means a MG Municipality’s (as hereinafter defined) annual plan for the activities to be financed by its allocation from the MG (as hereinafter defined);
- (b) “BM” means Banco de Moçambique, the Borrower’s central bank;
- (c) “DNDA” means the Borrower’s Directorate of Municipal Development within MAE (as hereinafter defined) ;
- (d) “Eligible Categories” means categories set forth in paragraph 5 of Part B of Schedule 1 to this Agreement;
- (e) “Eligible Expenditures” means the expenditures for works, goods and services referred to in Section 2.02 (a) of this Agreement and to be financed out of the proceeds of the Credit allocated from time to time to the Special Account’s respective Eligible Categories;
- (f) “Grant Board” means the oversight committee to be established by the Borrower for the purposes of Part B of the Project and referred to in Section 6.01 (g) of this Agreement;
- (g) “Grant Participation Agreement” means, for the purposes of Part B of this Project, the agreement to be entered into between the Borrower and a MG Municipality (as hereinafter defined), which sets out the rules for each MG (as hereinafter defined), referred to in Section 3.01 (d) of this Agreement;
- (h) “IMAP” means the Borrower’s Intermediate Institute of Public Administration;
- (i) “Initial Deposit” means the amount specified in Section 3.04 (b) of this Agreement;
- (j) “MAE” means the Borrower’s Ministry of State Administration;

(k) “Memorandum of Understanding” or “MOU” means the agreement between MAE and IMAP regarding their mutual obligations for the purposes of carrying out Part D of the Project;

(l) “Meticaís” means the Borrower’s currency;

(m) “MG” or “Municipal Grants” or “*Fundo de Subvenções Municipais*” means, for the purposes of Part B of the Project, the funding mechanism through which the Borrower will provide grants to a MG Municipality for eligible identified municipal activities to be financed in accordance with the provisions of Schedule 1 to this Agreement;

(n) “MG Municipality” means each one of the municipalities to receive their respective MG, all selected in accordance with the respective criteria specified in Schedule 4 to this Agreement;

(o) “MPF” means the Borrower’s Ministry of Planning and Finance;

(p) “Municipal Accounts” means the accounts referred to in paragraph 3 of Part B of Schedule 1 to this Agreement;

(q) “Municipal Project Accounts” means each one of the bank accounts that shall be opened for each one of the municipalities referred to in Section 3.04 (e) of this Agreement;

(r) “*Nucleos*” means the groups of consultants hired by each participating MG Municipality for the implementation of their respective MG.

(s) “PCU” means the Project Coordination Unit referred to in paragraph 2 (d) of Schedule 4 to this Agreement;

(t) “PIM” means the Borrower’s Project Implementation Manual referred to in paragraph 9 (a) of Part B of Schedule 1 to this Agreement, containing detailed arrangements regarding the implementation of the different activities under the Project, including, *inter alia*, the institutional responsibilities, reporting structure, review and monitoring, procurement, disbursement and financial management for the purposes of the implementation of the Project;

(u) “Project Account” means the account referred to in Section 3.04 (a) to this Agreement;

(v) “Project Management Report” means each report prepared in accordance with Section 4.02 of this Agreement;

(w) "Project Preparation Advance" means the project preparation advance granted by the Association to the Borrower pursuant to a letter signed on behalf of the Association on June 7, 1999 and on behalf of the Borrower on June 30, 1999;

(x) "Special Account" means the account referred to in Part B of Schedule 1 to this Agreement; and

(y) "Steering Committee" means the committee to be established for the purposes of Part A of the Project.

ARTICLE II

The Credit

Section 2.01. The Association agrees to lend to the Borrower, on the terms and conditions set forth or referred to in the Development Credit Agreement, an amount in various currencies equivalent to twenty-six million seven hundred thousand Special Drawing Rights (SDR26,700,000).

Section 2.02. (a) The amount of the Credit may be withdrawn from the Credit Account in accordance with the provisions of Schedule 1 to this Agreement for: (i) expenditures made (or, if the Association shall so agree, to be made) in respect of the reasonable cost of goods, works and services required for the Project described in Schedule 2 to this Agreement and to be financed out of the proceeds of the Credit; and (ii) amounts paid (or if the Association shall so agree, amounts to be paid) by the Borrower on account of withdrawals made for the benefit of municipalities under the MG, to meet the reasonable costs of goods, works and services required for such MG, and in respect of which withdrawal from the Credit Account is requested.

(b) Promptly after the Effective Date, the Association shall, on behalf of the Borrower, withdraw from the Credit Account and pay to itself the amount required to repay the principal amount of the Project Preparation Advance withdrawn and outstanding as of such date and to pay all unpaid charges thereon. The unwithdrawn balance of the authorized amount of the Project Preparation Advance shall thereupon be cancelled.

Section 2.03. The Closing Date shall be February 28, 2006, or such later date as the Association shall establish. The Association shall promptly notify the Borrower of such later date.

Section 2.04. (a) The Borrower shall pay to the Association a commitment charge on the principal amount of the Credit not withdrawn from time to time at a rate to be set by the Association as of June 30 of each year, but not to exceed the rate of one-half of one percent (1/2 of 1%) per annum.

(b) The commitment charge shall accrue: (i) from the date sixty days after the date of this Agreement (the accrual date) to the respective dates on which amounts shall be withdrawn by the Borrower from the Credit Account or canceled; and (ii) at the rate set as of the June 30 immediately preceding the accrual date and at such other rates as may be set from time to time thereafter pursuant to paragraph (a) above. The rate set as of June 30 in each year shall be applied from the next date in that year specified in Section 2.06 of this Agreement.

(c) The commitment charge shall be paid: (i) at such places as the Association shall reasonably request; (ii) without restrictions of any kind imposed by, or in the territory of, the Borrower; and (iii) in the currency specified in this Agreement for the purposes of Section 4.02 of the General Conditions or in such other eligible currency or currencies as may from time to time be designated or selected pursuant to the provisions of that Section.

Section 2.05. The Borrower shall pay to the Association a service charge at the rate of three-fourths of one percent ($3/4$ of 1%) per annum on the principal amount of the Credit withdrawn and outstanding from time to time.

Section 2.06. Commitment charges and service charges shall be payable semiannually on April 1 and October 1 in each year.

Section 2.07. (a) Subject to paragraphs (b), (c) and (d) below, the Borrower shall repay the principal amount of the Credit in semiannual installments payable on each April 1 and October 1 commencing October 1, 2011 and ending April 1, 2041. Each installment to and including the installment payable on April 1, 2021 shall be one percent (1%) of such principal amount, and each installment thereafter shall be two percent (2%) of such principal amount.

(b) Whenever: (i) the Borrower's per capita gross national product (GNP), as determined by the Association, shall have exceeded for three consecutive years the level established annually by the Association for determining eligibility to access the Association's resources; and (ii) the Association shall consider the Borrower creditworthy for Bank lending, the Association may, subsequent to the review and approval thereof by the Executive Directors of the Association and after due consideration by them of the development of the Borrower's economy, modify the repayment of installments under paragraph (a) above by:

- (A) requiring the Borrower to repay twice the amount of each such installment not yet due until the principal amount of the Credit shall have been repaid; and
- (B) requiring the Borrower to commence repayment of the principal amount of the Credit as of the first semiannual payment date referred to in paragraph (a) above falling six months or more after the date on which the Association notifies the Borrower that the

events set out in this paragraph (b) have occurred, provided, however, that there shall be a grace period of a minimum of five years on such repayment of principal.

(c) If so requested by the Borrower, the Association may revise the modification referred to in paragraph (b) above to include, in lieu of some or all of the increase in the amounts of such installments, the payment of interest at an annual rate agreed with the Association on the principal amount of the Credit withdrawn and outstanding from time to time, provided that, in the judgment of the Association, such revision shall not change the grant element obtained under the above-mentioned repayment modification.

(d) If, at any time after a modification of terms pursuant to paragraph (b) above, the Association determines that the Borrower's economic condition has deteriorated significantly, the Association may, if so requested by the Borrower, further modify the terms of repayment to conform to the schedule of installments as provided in paragraph (a) above.

Section 2.08. The currency of United States of America is hereby specified for the purposes of Section 4.02 of the General Conditions.

ARTICLE III

Execution of the Project

Section 3.01. (a) The Borrower declares its commitment to the objectives of the Project as set forth in Schedule 2 to this Agreement and, to this end: (i) shall carry out the Project with due diligence and efficiency and in conformity with appropriate financial, technical, administrative, engineering and environmental practices, and shall provide promptly as needed, the funds, facilities, services and other resources required for the Project; and (ii) without any limitation or restriction upon any of its other obligations under this Agreement, shall cause each MG Municipality to perform in accordance with the provisions of their individual Grant Participation Agreement all the obligations of the municipalities therein set forth, shall take and cause to be taken all actions, including the provision of funds, facilities, services and other resources, necessary or appropriate to enable the municipalities to perform such obligations, and shall not take or permit to be taken any action which would prevent or interfere with such performance;

(b) Without limitation upon the provisions of paragraph (a) of this Section and, except as the Borrower and the Association shall otherwise agree, the Borrower shall carry out the Project in accordance with the Implementation Program set forth in Schedule 4 to this Agreement;

(c) Without limitation upon the provisions of paragraph (a) of this Section and, except as the Borrower and the Association shall otherwise agree, the Borrower shall assist

the municipalities in carrying out Part B of the Project in accordance with the terms and conditions set forth in the Grant Participation Agreements; and

(d) For the purposes of Part B of the Project, the Borrower shall: (i) make available part of the proceeds of the Credit under Category 1, 2 (a) and 3 (b) of the table in paragraph A of Schedule 1 to this Agreement to the municipalities as grants under a subsidiary agreement to be entered into between the Borrower and each MG Municipality (the Grant Participation Agreement) under terms and conditions which shall have been approved by the Association; and (ii) exercise its rights under the Grant Participation Agreement in such manner as to protect the interests of the Borrower and the Association and to accomplish the purposes of the Project.

Section 3.02. Except as the Association shall otherwise agree, procurement of the goods, works and services required for the Project and to be financed out of the proceeds of the Credit shall be governed by the provisions of Schedule 3 to this Agreement.

Section 3.03. For the purposes of Section 9.07 of the General Conditions and without limitation thereto, the Borrower shall:

(a) prepare, on the basis of guidelines acceptable to the Association, and furnish to the Association not later than six months after the Closing Date or such later date as may be agreed for this purpose between the Borrower and the Association, a plan designed to ensure the sustainability of the Project; and

(b) afford the Association a reasonable opportunity to exchange views with the Borrower on said plan.

Section 3.04. Without limitation to its obligations under Section 3.01 of this Agreement, the Borrower shall:

(a) open and thereafter maintain, until the completion of the Project, an account (the Project Account) in Meticaïs, in a commercial bank acceptable to the Association;

(b) deposit, no later than 60 days after the Date of Effectiveness, an initial amount in Meticaïs equivalent to \$12,000 (Initial Deposit) into such account to finance the Borrower's contribution to the Project;

(c) thereafter deposit into the Project Account by the first day of each quarter each year during Project implementation such amounts as shall be required and agreed upon with the Association to timely replenish the Project Account back to the amount of the Initial Deposit referred to in paragraph (b);

(d) use the funds in the Project Account exclusively to finance expenditures under the Project; and

(e) cause each MG Municipality to: (i) open and maintain, in Meticaïs, in one or more commercial banks acceptable to the Association, a Municipal Project Account, in the name of each MG Municipality to be used by such MG Municipality as the MG Municipality's counterpart contribution to the costs of Part B of the Project; and (ii) deposit into each Municipal Project Account, an initial amount sufficient to cover the counterpart funds contribution to the Project for each MG Municipality as determined by its Annual MG Investment Plan.

ARTICLE IV

Financial Covenants

Section 4.01. (a) The Borrower shall maintain or cause to be maintained records and accounts adequate to reflect, in accordance with sound accounting practices, the operations, resources and expenditures in respect of the Project of the departments or agencies of the Borrower responsible for carrying out the Project or any part thereof.

(b) The Borrower shall:

- (i) have the records and accounts referred to in paragraph (a) of this Section, including those for the Special Account, for each fiscal year audited, in accordance with appropriate auditing principles consistently applied, by independent auditors acceptable to the Association;
- (ii) furnish to the Association as soon as available, but in any case not later than six months after the end of each such year, the report of such audit by said auditors, of such scope and in such detail as the Association shall have reasonably requested; and
- (iii) furnish to the Association such other information concerning said records and accounts and the audit thereof as the Association shall from time to time reasonably request.

(c) For all expenditures with respect to which withdrawals from the Credit Account were made on the basis of Project Management Reports, or statements of expenditure, the Borrower shall:

- (i) maintain or cause to be maintained, in accordance with paragraph (a) of this Section, records and separate accounts reflecting such expenditures;
- (ii) retain, until at least one year after the Association has received the audit report for the fiscal year in which the last withdrawal from the

Credit Account was made, all records (contracts, orders, invoices, bills, receipts and other documents) evidencing such expenditures;

- (iii) enable the Association's representatives to examine such records; and
- (iv) ensure that such records and accounts are included in the annual audit referred to in paragraph (b) of this Section and that the report of such audit contains a separate opinion by said auditors as to whether the Project Management Reports or statements of expenditure submitted during such fiscal year, together with the procedures and internal controls involved in their preparation, can be relied upon to support the related withdrawals.

Section 4.02. (a) Without limitation upon the provisions of Section 4.01 of this Agreement, the Borrower shall carry out a time-bound action plan for the strengthening of a financial management system acceptable to the Association in order to enable the Borrower, not later than eighteen months after the Effective Date, or such later date as the Association shall agree, to prepare quarterly Project Management Reports, acceptable to the Association, consisting of three separate, but coherent reports of which:

- (i) the financial report: (A) sets forth actual sources and applications of funds for the Project, both cumulatively and for the period covered by said report, and projected sources and applications of funds for the Project for the six-month period following the period covered by said report; and (B) shows separately expenditures financed out of the proceeds of the Credit during the period covered by said report and expenditures proposed to be financed out of the proceeds of the Credit during the six-month period following the period covered by said report;
- (ii) the status report describes: (A) physical progress in Project implementation, both cumulatively and for the period covered by said report; and (B) explains variances between the actual and previously forecast implementation targets, as the case may be; and
- (iii) the procurement report sets forth the status of procurement under the Project and expenditures under contracts financed out of the proceeds of the Credit, as at the end of the period covered by said report.

(b) Upon the completion of the action plan referred to in paragraph (a) of this Section, the Borrower shall prepare, in accordance with guidelines acceptable to the Association, and furnish to the Association not later than 45 days after the end of each calendar quarter a Project Management Report for such period.

ARTICLE V

Remedies of the Association

Section 5.01. Pursuant to Section 6.02 (l) of the General Conditions, the following additional event is specified, namely, that the Borrower's (i) Municipal Legislation (*Pacote Autárquico*) or Law of the municipalities (Law No. 2 of February 18, 1997), the Law of Municipal Finances (Law No. 11 of May 31, 1997) and Law No. 9 of November 22, 1996, and (ii) Municipal Tax Code or Decree No. 52/2000, shall have been amended, suspended, abrogated, repealed or waived so as to affect materially and adversely the ability of the Borrower and the municipalities to perform any of their obligations under their respective Grant Participation Agreement.

Section 5.02. Pursuant to Section 7.01 (h) of the General Conditions, the following additional event is specified, namely that the event specified in Section 5.01 of this Agreement shall occur and shall continue for a period of 60 days after notice thereof shall have been given by the Association to the Borrower.

ARTICLE VI

Effective Date; Termination

Section 6.01. The following events are specified as additional conditions to the effectiveness of this Agreement within the meaning of Section 12.01 (b) of the General Conditions:

(a) the auditors referred to in Section 4.01 (b) (i) of this Agreement have been appointed on terms of reference acceptable to the Association and in accordance with the provisions of Section II of Schedule 3 to this Agreement;

(b) the Borrower has established a financial management system, in form and substance acceptable to the Association, including the development of a financial procedures manual and the appointment of financial management staff for the Municipal *Nucleos* and PCU with experience acceptable to the Association;

(c) Grant Participation Agreements have been signed between the Borrower and at least three municipalities and evidence has been furnished satisfactory to the Association that such agreements are binding upon the respective MG Municipality in accordance with its terms;

(d) the Memorandum of Understanding has been signed between IMAP and MAE;

(e) the Borrower has employed the Project Director and the consulting firm that will provide the staff for the PCU, in accordance with the provisions of Schedule 3 to this Agreement;

(f) the Project Account has been opened; and

(g) the Grant Board members have been officially appointed and the Grant Board has held its first meeting.

Section 6.02. The date ninety (90) days after the date of this Agreement, is hereby specified for the purposes of Section 12.04 of the General Conditions.

ARTICLE VII

Representative of the Borrower; Addresses

Section 7.01. The Governor of the Bank of Mozambique is designated as representative of the Borrower for the purposes of Section 11.03 of the General Conditions.

Section 7.02. The following addresses are specified for the purposes of Section 11.01 of the General Conditions:

For the Borrower:

Governor
Banco de Moçambique
Departamento de Estrangeiro
Maputo
Republic of Mozambique

Cable address:	Telex:	Facsimile:
MOBANCO	6355/BMMO	258 1 428565

For the Association:

International Development Association
1818 H Street, NW
Washington, D.C. 20433
United States of America

Cable address:	Telex:	Facsimile:
INDEVAS Washington, D.C.	248423 (MCI) or 64145 (MCI)	(202) 477 6391

IN WITNESS WHEREOF, the parties hereto, acting through their duly authorized representatives, have caused this Agreement to be signed in their respective names in the District of Columbia, United States of America, as of the day and year first above written.

REPUBLIC OF MOZAMBIQUE

By: /s/ Ismael Valigy
Authorized Representative

INTERNATIONAL DEVELOPMENT ASSOCIATION

By: /s/ Theodore Ahlers
Acting Regional Vice President
Africa

SCHEDULE 1

Withdrawal of the Proceeds of the Credit

A. General

1. The table below sets forth the Categories of items to be financed out of the proceeds of the Credit, the allocation of the amounts of the Credit to each Category and the percentage of expenditures for items so to be financed in each Category:

<u>Category</u>	<u>Amount of the Credit Allocated (Expressed in SDR Equivalent)</u>	<u>% of Expenditures to be Financed</u>
1. Works for Part B of the Project	10,250,000	85%
2. Goods and equipment including vehicles for:		100% of foreign expenditures and 85% of local expenditures
(a) Part B of the Project	4,470,000	
(b) Part C of the Project	100,000	
3. Consultants' services, training, and studies for:		
(a) Part A of the Project	2,840,000	100%
(b) Part B of the Project	1,220,000	85%
(c) Part C of the Project including audits	4,470,000	100%

<u>Category</u>	<u>Amount of the Credit Allocated (Expressed in SDR Equivalent)</u>	<u>% of Expenditures to be Financed</u>
4. Incremental Operating Costs for Part C of the Project	710,000	85% of local expenditures
5. Refinancing of the Project Preparation Advance	710,000	Amounts due pursuant to Section 2.02 (b) of this Agreement
6. Unallocated	1,930,000	
TOTAL	<u><u>26,700,000</u></u>	

2. For the purposes of this Schedule:

(a) the term “foreign expenditures” means expenditures in the currency of any country other than that of the Borrower for goods or services supplied from the territory of any country other than that of the Borrower;

(b) the term “local expenditures” means expenditures in the currency of the Borrower or for goods or services supplied from the territory of the Borrower; and

(c) the term “Incremental Operating costs” means the incremental expenses incurred by the Borrower on account of the Project implementation including office supplies, fuel and maintenance for official Project vehicles, maintenance of office equipment, in-country travel, accommodations and subsistence for Project-related business, and communications for project-related business, but excluding salaries of officials or staff of the Borrower.

3. Notwithstanding the provisions of paragraph 1 above, no withdrawals shall be made in respect of payments made for expenditures prior to the date of this Agreement or:

(a) payments made under Category 3 (a) of the table in paragraph A.1 of this Schedule until: (i) MAE has appointed an official to manage the implementation of Part A of the Project; (ii) the Borrower has designated a Steering Committee for the implementation of Part A of the Project; and (iii) the Steering Committee has held its first meeting;

(b) payments made under Category 1, 2 (a) and 3 (b) of the table in paragraph A.1 of the Schedule for each MG Municipality until: (i) the respective MG Municipality has executed its Grant Participation Agreement with MAE; (ii) the MG Municipality's Municipal Project Accounts have been opened and the counterpart funds deposited accordingly; (iii) the respective MG Municipality has complied with MG eligibility requirements in Schedule 4 to this Agreement; (iv) the respective MG Municipality has appointed staff for its respective *Nucleo* acceptable to the Association; (v) the MG Municipality's Project Accounts for the previous year have been audited; and (vi) the MG Municipality counterpart funds for the MG have been budgeted in the following year's budget; and

(c) payments made under Category 1, 2 (a) and 3 (b) of the table in paragraph A.1 of the Schedule for: (i) Maputo until its respective Project Account has been opened and the amount equivalent to \$14,000 (counterpart contribution) has been deposited accordingly; (ii) Beira until its respective Project Account has been opened and the amount equivalent to \$10,000 (counterpart contribution) has been deposited accordingly; (iii) Nampula until its respective Project Account has been opened and the amount equivalent to \$10,000 (counterpart contribution) has been deposited accordingly; (iv) Quelimane until its respective Project Account has been opened and the amount equivalent to \$7,000 (counterpart contribution) has been deposited accordingly; and (v) Pemba until its respective Project Account has been opened and the amount equivalent to \$7,000 (counterpart contribution) has been deposited accordingly.

4. The Association may require withdrawals from the Credit Account to be made on the basis of statements of expenditure for expenditures under: (a) contracts for goods costing (i) less than \$100,000 equivalent each during the first year of the Project, and (ii) less than \$200,000 from the second year of the Project and onwards; (b) contracts for consulting firms costing less than \$100,000 equivalent each; (c) contracts for individual consultants costing less than \$50,000 equivalent each; (d) works costing: (i) less than \$100,000 during the first year of the Project; and (ii) less than \$250,000 from the second year of the Project and onwards; and (e) all operating costs and training as the Association shall determine.

B. Special Account

1. The Borrower shall, for the purposes of the Project, open and maintain in US Dollars a special deposit account in a commercial bank acceptable to the Association, on terms and conditions satisfactory to the Association, including appropriate protection against set-off, seizure and attachment.
2. After the Association has received evidence satisfactory to it that the Special Account has been opened, withdrawals from the Credit Account of amounts to be deposited into the Special Account shall be made as follows:

(a) until the Association shall have received: (i) the first Project Management Report referred to in Section 4.02 (b) of this Agreement; and (ii) a request from the

Borrower for withdrawal on the basis of Project Management Reports, withdrawals shall be made in accordance with the provisions of Annex A to this Schedule 1; and

(b) upon receipt by the Association of a Project Management Report pursuant to Section 4.02 (b) of this Agreement, accompanied by a request from the Borrower for withdrawal on the basis of Project Management Reports, all further withdrawals shall be made in accordance with the provisions of Annex B to this Schedule 1.

3. Promptly after the Effectiveness Date the Borrower shall:

(a) open and maintain in Dollars Municipal Accounts, for each of the municipalities where commercial banks are available, in a commercial bank acceptable to the Association, on terms and conditions acceptable to the Association (including appropriate protection against set-off, seizure or attachment), to be used by such municipalities exclusively for the purposes of financing MG under Part B of the Project to be carried out by such MG Municipality; and

(b) withdraw from the Special Account and deposit into each Municipal Account an amount not exceeding \$160,000 for Maputo, \$140,000 for Beira, \$120,000 for Nampula, \$80,000 for Quelimane and \$80,000 for Pemba and thereafter replenish said Municipal Accounts in accordance with Schedule 1 to this Agreement.

4. Payments out of the Special Account shall be made exclusively for Eligible Expenditures in accordance with the provisions of this Schedule. For each payment made by the Borrower out of the Special Account or out of any of the Municipal Accounts, the Borrower shall, at such time as the Association shall reasonably request, furnish to the Association such documents and other evidence showing that such payment was made exclusively for Eligible Expenditures.

5. For the purposes of this Schedule, the term "Eligible Categories" means Categories (1) through (4) set forth in the table in paragraph 1 of this Schedule 1.

6. Notwithstanding the provisions of Part B.2 of this Schedule, the Association shall not be required to make further deposits into the Special Account:

(a) if the Association determines at any time that all further withdrawals should be made by the Borrower directly from the Credit Account; or

(b) if the Borrower shall have failed to furnish to the Association within the period of time specified in Section 4.01 (b) (ii) of this Agreement, any of the audit reports required to be furnished to the Association pursuant to said Section in respect of the audit of: (A) the records and accounts for the Special Account, or (B) the records and accounts reflecting expenditures with respect to which withdrawals were made on the basis of Project Management Reports.

7. The Association shall not be required to make further deposits into the Special Account in accordance with the provisions of Part B.2 of this Schedule if, at any time, the

Association shall have notified the Borrower of its intention to suspend in whole or in part the right of the Borrower to make withdrawals from the Credit Account pursuant to Section 6.02 of the General Conditions. Upon such notification, the Association shall determine, in its sole discretion, whether further deposits into the Special Account may be made and what procedures should be followed for making such deposits, and shall notify the Borrower of its determination.

8. (a) If the Association determines at any time that any payment out of the Special Account or out of any of the Municipal Accounts was made for an expenditure which is not an Eligible Expenditure, or was not justified by the evidence furnished to the Association, the Borrower shall, promptly upon notice from the Association, provide such additional evidence as the Association may request, or deposit into the Special Account or the respective Municipal Account (or, if the Association shall so request, refund to the Association) an amount equal to the amount of such payment. Unless the Association shall otherwise agree, no further deposit by the Association into the Special Account or the respective Municipal Account shall be made until the Borrower has provided such evidence or made such deposit or refund, as the case may be.

(b) If the Association determines at any time that any amount outstanding in the Special Account will not be required to cover payments for Eligible Expenditures during the six-month period following such determination, the Borrower shall, promptly upon notice from the Association, refund to the Association such outstanding amount.

(c) The Borrower may, upon notice to the Association, refund to the Association all or any portion of the funds on deposit in the Special Account.

(d) Refunds to the Association made pursuant to sub-paragraph (a), (b) or (c) of this paragraph 7 shall be credited to the Credit Account for subsequent withdrawal or for cancellation in accordance with the provisions of the Development Credit Agreement.

9. (a) The Borrower shall withdraw from the Special Account and deposit into each Municipal Account the funds to assist the municipalities to pay for MG under Part B of the Project. Such withdrawals or deposits shall be in amounts sufficient to assist each municipality to pay for such MG provided that in no event the Borrower shall cause the amount held in any Municipal Account to exceed the amounts determined by the PCU in accordance with the PIM or the equivalent of: (i) \$350,000 for Maputo; (ii) \$300,000 for Beira; (iii) \$200,000 for Nampula; (iv) \$200,000 for Quelimane; and (v) \$150,000 for Pemba, whichever is the smaller;

(b) payments out of any Municipal Account shall only be made for eligible expenditures under categories 1, 2 (a) and 3 (b) as set forth in the table in Section A.1 of Schedule 1 to this Agreement;

(c) withdrawals from any Municipal Account may be justified by the Borrower on the basis of statements of expenditures for eligible expenditures under the MG including (i) works estimated to cost less than \$100,000 equivalent, (ii) goods estimated to cost less than \$100,000 equivalent, and (iii) consultant services costing less than \$20,000 equivalent; and

(d) in the event the Association, after consultation with the Borrower, determines that any outstanding amount in any Municipal Account is not further required to cover payments for eligible expenditures, the MG Municipality beneficiary of such Municipal Account, upon notice from the Association, shall promptly refund such outstanding amount to the Special Account.

Annex A
to
SCHEDULE 1
Operation of Special Account
When Withdrawals Are Not Made
On the Basis of Project Management Reports

1. For the purposes of this Annex:

The term “Authorized Allocation” means an amount of \$1,600,000 to be withdrawn from the Credit Account and deposited into the Special Account pursuant to paragraph 2 of this Annex; provided, however, that unless the Association shall otherwise agree, the Authorized Allocation shall be limited to an amount of \$1,000,000 until the aggregate amount of withdrawals from the Credit Account, plus the total amount of all outstanding special commitments entered into by the Association pursuant to Section 5.02 of the General Conditions shall equal or exceed the equivalent of SDR 5,000,000.

2. Withdrawals of the Special Account’s Authorized Allocation and subsequent withdrawals to replenish said Special Account shall be made as follows:

- (a) For withdrawals of the Special Account’s Authorized Allocation, the Borrower shall furnish to the Association a request or requests for deposit into the Special Account of an amount or amounts which in the aggregate do not exceed the Authorized Allocation. On the basis of each such request, the Association shall, on behalf of the Borrower, withdraw from the Credit Account and deposit into the Special Account such amount as the Borrower shall have requested.

- (b) For replenishment of the Special Account, the Borrower shall furnish to the Association requests for deposit into the Special Account at such intervals as the Association shall specify. Prior to or at the time of each such request, the Borrower shall furnish to the Association the documents and other evidence required pursuant to Part B.3. of Schedule 1 to this Agreement for the payment or payments in respect of which replenishment is requested. On the basis of each such request, the Association shall, on behalf of the Borrower, withdraw from the Credit Account and deposit into the Special Account such amount as the Borrower shall have requested and as shall have been shown by the documents and other evidence to have been paid out of the Special Account for Eligible Expenditures. Each such deposit into the Special Account shall be withdrawn by the Association from the Credit Account under one or more of the Special Account’s Eligible Categories.

3. The Association shall not be required to make further deposits into the Special Account, once the total unwithdrawn amount of the Credit minus the total amount of all outstanding special commitments entered into by the Association pursuant to Section 5.02 of the General Conditions, shall equal the equivalent of twice the amount of the Special Account’s Authorized Allocation. Thereafter, withdrawal from the Credit Account of the

remaining unwithdrawn amount of the Credit shall follow such procedures as the Association shall specify by notice to the Borrower. Such further withdrawals shall be made only after and to the extent that the Association shall have been satisfied that all such amounts remaining on deposit in the Special Account as of the date of such notice will be utilized in making payments for Eligible Expenditures.

Annex B
to
SCHEDULE 1
Operation of Special Account
When Withdrawals Are Made
On the Basis of Project Management Reports

1. Except as the Association may otherwise specify by notice to the Borrower, all withdrawals from the Credit Account shall be deposited by the Association into the Special Account in accordance with the provisions of Schedule 1 to this Agreement. Each such deposit into the Special Account shall be withdrawn by the Association from the Credit Account under one or more of the Special Account's Eligible Categories.
2. Each application for withdrawal from the Credit Account for deposit into the Special Account shall be supported by a Project Management Report.
3. Upon receipt of each application for withdrawal of an amount of the Credit, the Association shall, on behalf of the Borrower, withdraw from the Credit Account and deposit into the Special Account an amount equal to the lesser of: (a) the amount so requested; and (b) the amount which the Association has determined, based on the Project Management Report accompanying said application, is required to be deposited in order to finance Eligible Expenditures during the six-month period following the date of such report; provided, however, that the amount so deposited, when added to the amount indicated by said Project Management Report to be remaining in the Special Account, shall not exceed the amount of three million seven hundred thousand US Dollars (US\$3,700,000).

SCHEDULE 2

Description of the Project

The objectives of the Project are to assist the Borrower in: (i) operationalizing the legal and institutional framework for municipal governance; and (ii) establishing and operating a mechanism for providing grants to municipalities through a pilot program in five cities in the Borrower's territory to finance capital investments for municipal capacity building and infrastructure.

The Project consists of the following Parts, subject to such modifications thereof as the Borrower and the Association may agree upon from time to time to achieve such objectives:

Part A: Legal and Institutional Reform

1. Carrying out studies of the legislation and regulations governing the recruitment, management and mobility of municipal staff, including the identification of the legal instruments that will require revision and the development of an action plan for drafting them, through the provision of technical advisory services.
2. Drafting legal instruments to: (i) regulate municipal budgets; (ii) establish municipal financial management, accounting and auditing rules for municipal finance; (iii) regulate revenue collection; (iv) regulate municipal expenditure management; and (v) regulate training of municipal officials and staff, all through the provision of technical advisory services.
3. Review of the Municipal Legislation (*Pacote Autárquico*), including the Laws No. 02 and 11 of 1997 and the Municipal Tax Code, to identify and propose amendments to the legislation, through the provision of technical advisory services.
4. Review of drafts of the model Municipal Ordinances Code and the decree for transfer of responsibilities from the state to the municipalities, through the provision of technical advisory services.
5. Carrying out case-by-case analyses of proposals for transfer of specific responsibilities from Borrower's Government central agencies to the municipalities and drafting the legal instruments for effecting such transfers, through the provision of technical advisory services.
6. (a) Carrying out studies, defining mechanisms and drafting the basis of legal instruments for public investments in the municipalities and the repartition of public investments between the state and the municipalities; and (b) drafting of manuals for the programming of public investments, through the provision of technical advisory services.
7. Carrying out studies on the provision and administration of municipal services and drafting legal instruments to regulate municipal autonomous public services, public

investments, municipal public enterprises and the assignment of the responsibilities for public infrastructure from the State to the municipalities.

8. Developing mechanisms for taxes and fees collection and drafting of a manual for the implementation of a municipal tax cadastre, through the provision of technical advisory services.

9. (a) Carrying out a diagnostic study of the staffing situation in the Borrower's municipalities and developing model staffing tables as guidelines for municipal governments; and (b) drafting a manual for the recruitment, selection and employment conditions of municipal staff, through the provision of technical advisory services.

10. Carrying out a diagnostic study of the management structures and financial management of the municipal governments, including: (a) drafting a manual for the elaboration, supervision and execution of: (i) municipal development plans; and (ii) annual action plans; and (b) drafting of manuals for the preparation, execution and monitoring of municipal budgets, through the provision of technical advisory services.

11. Developing a methodology for the promotion and consideration of community participation in municipal decision-making, through the provision of technical advisory services.

12. Building capacities of MAE and MPF to publicize, explain, interpret and clarify legal instruments to the municipalities and other bodies, through the provision of technical advisory services.

13. Institutional support to the Borrower's municipalities for starting the implementation of new laws and regulations, through the provision of technical advisory services.

Part B: Municipal Grants

Provision of grants to the Borrower's municipalities for the: (i) rehabilitation and expansion of infrastructure; (ii) purchase of equipment and materials for the provision of municipal basic services and management; and (iii) provision of technical advisory services to improve municipal management, finances and services.

Part C: Project Management and Technical Assistance

1. Carrying out project management, financial management, contract management, supervision, monitoring and procurement activities through the provision of technical advisory services to staff the Project Coordination Unit.

2. Technical support to the Borrower's municipalities participating in the MG in infrastructure engineering, project financial management and procurement, through the provision of technical advisory services through the Grants Unit of the Project Coordination Unit.

Part D: Capacity Building

1. Establishment of a permanent unit for planning and management of training and technical assistance for the municipalities through the provision of technical advisory services financed by the NDF Credit Agreement.

2. Implementation of training courses for municipal officials and staff in: (i) the functioning of the municipal government system; (ii) planning and management of basic public services and infrastructure; (iii) principles of financial planning and budgeting for municipalities; (iv) environmental management; (v) basic structure of municipal government in Mozambique; (vi) specialized courses in the duties and responsibilities of the selected posts; and (vii) municipal finance and delivery of basic services, through the provision of technical advisory services financed by the NDF Credit Agreement.

3. Periodic reviews of needs and impacts of training and technical assistance by central and municipal authorities, through the provision of technical advisory services financed by the NDF Credit Agreement.

4. Preparation of materials for courses to be offered at vocational school, university and graduate level to qualify candidates for management and technical staff positions in the municipalities, through the provision of technical advisory services financed by the NDF Credit Agreement.

* * *

The Project is expected to be completed by August 31, 2005.

SCHEDULE 3

Procurement and Consultants' Services

Section I. Procurement of Good and Works

Part A: General

1. Goods and works shall be procured in accordance with the provisions of Section I of the "Guidelines for Procurement under IBRD Loans and IDA Credits" published by the Association in January 1995 and revised in January and August 1996, September 1997 and January 1999 (the Guidelines) and the following provisions of Section I of this Schedule.
2. In paragraphs 1.6 and 1.8 of the Guidelines, the references to "Bank member countries" and "member country" shall be deemed to be references, respectively, to "Participating Countries" and "Participating Country".

Part B: International Competitive Bidding

1. Except as otherwise provided in Part C of this Section, goods and works shall be procured under contracts awarded in accordance with the provisions of Section II of the Guidelines and paragraph 5 of Appendix 1 thereto.
2. The following provisions shall apply to goods and works to be procured under contracts awarded in accordance with the provisions of paragraph 1 of this Part B.

(a) Grouping of contracts

To the extent practicable, contracts for works and goods shall be grouped in bid packages estimated to cost \$200,000 equivalent or more each.

(b) Preference for domestically manufactured goods and domestic contractors

The provisions of paragraphs 2.54 and 2.55 of the Guidelines and Appendix 2 thereto shall apply to goods manufactured in the territory of the Borrower and works to be carried out by domestic contractors.

(c) Notification and Advertising

The invitation to prequalify or bid for each contract estimated to cost \$500,000 equivalent or more shall be advertised in accordance with the procedures applicable to large contracts under paragraph 2.8 of the Guidelines.

Part C: Other Procurement Procedures

1. National Competitive Bidding

Goods estimated to cost less than \$200,000 and works estimated to cost less than \$500,000 equivalent per contract, up to an aggregate amount not to exceed \$500,000 equivalent for goods and \$17,000,000 for works, may be procured under contracts awarded in accordance with the provisions of paragraphs 3.3 and 3.4 of the Guidelines.

2. International or National Shopping

Goods estimated to cost less than \$30,000 equivalent per contract, up to an aggregate amount not to exceed \$1,500,000 equivalent, may be procured under contracts awarded on the basis of international or national shopping procedures in accordance with the provisions of paragraphs 3.5 and 3.6 of the Guidelines.

3. Procurement from UN Agencies

Vehicles and office equipment may be procured from UN agencies in accordance with the provisions of paragraph 3.9 of the Guidelines.

4. Procurement of Small Works

Works estimated to cost less than \$30,000 equivalent per contract, up to an aggregate amount not to exceed \$500,000 equivalent, may be procured under lump-sum, fixed-price contracts awarded on the basis of quotations obtained from three (3) qualified domestic contractors in response to a written invitation. The invitation shall include a detailed description of the works, including basic specifications, the required completion date, a basic form of agreement acceptable to the Bank, and relevant drawings, where applicable. The award shall be made to the contractor who offers the lowest price quotation for the required work, and who has the experience and resources to complete the contract successfully.

Part D: Review by the Bank of Procurement Decisions

1. Procurement Planning

Prior to the issuance of any invitations to pre-qualify for bidding or to bid for contracts, the proposed procurement plan for the Project shall be furnished to the Bank for its review and approval, in accordance with the provisions of paragraph 1 of Appendix 1 to the Guidelines. Procurement of all goods and works shall be undertaken in accordance with such procurement plan as shall have been approved by the Bank, and with the provisions of said paragraph 1.

2. Prior Review

(a) With respect to: (i) each contract for goods and works estimated to cost the equivalent of \$200,000 and \$250,000 respectively or more; and (ii) all contracts for goods and works in the first year estimated to cost the equivalent of \$100,000 or more, the procedures set forth in paragraphs 2 and 3 of Appendix 1 to the Guidelines shall apply.

(b) With respect to the first two contracts in each MG Municipality for goods and works exceeding the equivalent of \$30,000, the following procedures shall apply:

- (i) prior to the selection of any supplier under international or national shopping procedures, the Recipient shall provide to the Bank a report on the comparison and evaluation of quotations received;
- (ii) prior to the execution of any contract procured under direct contracting or international or national shopping procedures, the Recipient shall provide to the Bank a copy of the specifications and the draft contract; and
- (iii) the procedures set forth in paragraphs 2(f), 2(g) and 3 of Appendix 1 to the Guidelines shall apply.

3. Post Review

With respect to each contract not governed by paragraph 2 of this Part, the procedures set forth in paragraph 4 of Appendix 1 to the Guidelines shall apply.

Section II. Employment of Consultants

Part A: General

1. Consultants' services shall be procured in accordance with the provisions of the Introduction and Section IV of the "Guidelines: Selection and Employment of Consultants by World Association Borrowers" published by the Association in January 1997 and revised in September 1997 and January 1999 (the Consultant Guidelines) and the following provisions of Section II of this Schedule.

2. In paragraphs 1.10 of the Consultant Guidelines, the reference to "Bank member countries" and "member country" shall be deemed to be references, respectively, to "Participating Countries" and "Participating Country".

Part B: Quality- and Cost-based Selection

1. Except as otherwise provided in Part C of this Section, consultants' services shall be procured under contracts awarded in accordance with the provisions of Section II of the Consultant Guidelines, paragraph 3 of Appendix 1 thereto, Appendix 2 thereto, and the provisions of paragraphs 3.13 through 3.18 thereof applicable to quality- and cost-based selection of consultants.

2. The following provisions shall apply to consultants' services to be procured under contracts awarded in accordance with the provisions of the preceding paragraph. The short list of consultants for services estimated to cost less than \$200,000 equivalent per contract, may comprise entirely national consultants in accordance with the provisions of paragraph 2.7 of the Consultant Guidelines.

Part C: Other Procedures for the Selection of Consultants

1. Selection Based on Consultants' Qualifications

Selected services estimated to cost less than \$100,000 equivalent per contract may be procured under contracts awarded in accordance with the provisions of paragraphs 3.1 and 3.7 of the Consultant Guidelines.

2. Single Source Selection

Services for selected contracts which are estimated to cost less than \$100,000 equivalent per contract, may, with the Bank's prior agreement, be procured in accordance with the provisions of paragraphs 3.8 through 3.11 of the Consultant Guidelines.

3. Individual Consultants

Services for selected contracts as needed that meet the requirements set forth in paragraph 5.01 of the Consultant Guidelines shall be procured under contracts awarded to individual consultants in accordance with the provisions of paragraphs 5.1 through 5.3 of the Consultant Guidelines.

Part D: Review by the Bank of the Selection of Consultants

1. Selection Planning

Prior to the issuance to consultants of any requests for proposals, the proposed plan for the selection of consultants under the Project shall be furnished to the Bank for its review and approval, in accordance with the provisions of paragraph 1 of Appendix 1 to the Consultant Guidelines. Selection of all consultants' services shall be undertaken in accordance with such selection plan as shall have been approved by the Bank, and with the provisions of said paragraph 1.

2. Prior Review

(a) With respect to each contract for the employment of consulting firms estimated to cost the equivalent of \$200,000 or more, the procedures set forth in paragraphs 1, 2 (other than the third subparagraph of paragraph 2(a)) and 5 of Appendix 1 to the Consultant Guidelines shall apply.

(b) With respect to each contract for the employment of consulting firms estimated to cost the equivalent of \$100,000 or more, but less than the equivalent of \$200,000, the procedures set forth in paragraphs 1, 2 (other than the second subparagraph of paragraph 2(a)) and 5 of Appendix 1 to the Consultant Guidelines shall apply.

(c) With respect to each contract for the employment of individual consultants estimated to cost the equivalent of \$50,000 or more, the qualifications, experience, terms of reference and terms of employment of the consultants shall be furnished to the Bank for its prior review and approval. The contract shall be awarded only after said approval shall have been given.

3. Post Review

With respect to each contract not governed by paragraph 1 of this Part, the procedures set forth in paragraph 4 of Appendix 1 to the Consultant Guidelines shall apply.

SCHEDULE 4

Implementation Program

1. The Borrower shall:

(a) maintain policies and procedures adequate to enable it to monitor and evaluate on an ongoing basis, in accordance with the indicators set forth in Schedule 5 to this Agreement, the carrying out of the Project and the achievement of the objectives thereof;

(b) prepare, under terms of reference satisfactory to the Association, and furnish to the Association not later than sixty days after the end of each calendar year of each year of Project implementation, a report integrating the results of the monitoring and evaluation activities performed pursuant to paragraph (a) of this Section, on the progress achieved in the carrying out of the Project during the calendar year preceding the date of said report (provided, however, that the first report to be furnished to the Association shall cover the period from the date of effectiveness, through December 31, 2002), and setting out the measures recommended to ensure the efficient carrying out of the Project and the achievement of the objectives thereof during the period following such date;

(c) review with the Association, within 30 days of submission, or such later date as the Association shall request, the report referred to in paragraph (b) of this Section, and, thereafter, take all measures required to ensure the efficient completion of the Project and the achievement of the objectives thereof, based on the conclusions and recommendations of the said report and the Association's views on the matter; and

(d) establish a Steering Committee composed of representatives of entities, as agreed with the Association, to provide interagency coordination and guidance for the purposes of Part A of the Project.

2. Implementation under Part B of the Project:

(a) establish a Grant Board composed of representatives of entities as agreed with the Association to: (i) perform quarterly and annual reviews of the MG; (ii) perform annual evaluation of the MG; and (iii) review and decide on eligibility and suspension of municipalities to participate in the MG.

(b) PIM

Except as the Association shall otherwise agree, each MG Municipality shall apply the procedures and guidelines set out in the PIM, and the Borrower shall not assign, amend, abrogate or waive the PIM or any provision thereof which, in the opinion of the Association, will materially or adversely affect the implementation of the Project.

(c) For each MG Municipality that participates in the MG, the Borrower shall enter into a Grant Participation Agreement with a MG Municipality legally constituted under

Law 9/96 of November 22, 1996, Law 2/97 of February 18, 1997, and Law 7/97 of May 31, 1997. The terms and conditions of the Grant Participation Agreement shall include provisions pursuant to which:

- (i) each MG Municipality shall be responsible for complying with the provisions of the Grant Participation Agreement;
- (ii) each MG Municipality shall be responsible for implementing its Grant Participation Agreement in accordance with the provisions of the PIM, with due diligence and efficiency in accordance with sound technical, financial, environmental and managerial standards, and for maintaining adequate records;
- (iii) each MG Municipality shall have the obligation to report to the PCU of the MDP on a quarterly and annual basis on the financial status of the funds provided to it under the MG and the implementation of the activities financed by such funds;
- (iv) each MG Municipality shall provide to the Association all information as it shall reasonably request regarding the Municipality's general finances and administration and its use of the funds provided to it under the MG, and shall allow authorized representatives of the Association to inspect sub-projects financed by the MG and to have access to related facilities, records, and documents as well as information on the benefits to be derived from the activities funded by the MG;
- (v) the goods, civil works and services to be financed out of the proceeds of the MG shall be procured in accordance with the provisions of Schedule 3 to this Agreement;
- (vi) the MAE shall have the right to suspend or terminate the right of the MG Municipality to use the proceeds of the MG upon failure by any such MG Municipality to perform any of its respective obligations under the Grant Participation Agreement; and
- (vii) each MG Municipality shall maintain a team of officials and staff dedicated to the MDP, acceptable to the Association; and
- (viii) each MG Municipality shall fully cooperate with the annual audits of the MDP and make available all documents and data as the auditors may reasonably request.

(d) Any MG Municipality which fails to meet the eligibility requirements, as specified in the PIM, for an initial or a subsequent 12-month allocation from the MG within the time stipulated, will be disqualified from participation in the MG during that cycle, and another MG Municipality or Municipalities will be invited to participate.

3. Midterm Review

The Borrower shall:

(a) maintain policies and procedures adequate to enable it to monitor and evaluate on an ongoing basis, in accordance with the Performance Indicators specified in Schedule 5 to this Agreement, the carrying out of the Project and the achievement of the objectives thereof;

(b) carry out, jointly with the Association, not later than 24 months after the Effectiveness Date, a Midterm Review of the Project, which shall cover, inter alia: (i) progress made in meeting the Project's objectives; (ii) overall Project performance as measured against Performance Indicators; (iii) the adequacy of the institutional and management arrangements for the project and its components; and (iv) the operational efficiency and effectiveness of the Municipal Grants and the performance of the municipalities and their contractors under the MG;

(c) at least three (3) weeks prior to the Midterm Review, furnish to the Association a report describing the status of the items listed in paragraph (a) above and of Project implementation generally; and

(d) not later than four (4) weeks after the Midterm Review, prepare an action program, acceptable to the Association, for further implementation of the Project having regard to the findings of the Midterm Review and, thereafter, implement such action program.

SCHEDULE 5

Performance Indicators

Legal and Institutional Reform Component:

1. Legal instruments elaborated and submitted for approval by the appropriate higher authorities concerning: (i) recruitment, management and mobility of municipal staff; (ii) municipal budgets, financial management, accounting, and auditing; (iii) municipal revenue collection; (iv) the transfer of responsibilities and resources (e.g. for primary education and primary health) to the municipalities; and (vi) private municipal service providers and municipal public enterprises.
2. Studies undertaken and manuals prepared and disseminated for (i) recruitment, selection and employment of municipal staff (prepared in coordination with the Ministry of Planning and Finance); (ii) improving municipal financial management and revenue systems; (iii) preparation, supervision, and execution of municipal development plans and municipal annual action plans; and (iv) community participation in municipal decision-making.
3. Long-term program of municipal development elaborated in collaboration with governmental, municipal, civil society, and donor stakeholders.

Capacity-Building Component:

1. GCM established in IMAP and plans in place for continued existence of GCM at project close.
2. Strategy for training for municipalities developed and under implementation with linkages to the Government's public sector reform program and SIFAP.
3. Target numbers of municipal elected and appointed officials and municipal staff trained (see detailed project description for exact targets).

Municipal Grants:

1. Municipalities implement yearly investment activities (works, goods, consultancies) according to the guidelines of the MG, procuring civil works contractors (firms), suppliers for the purchase of equipment, and consultants for technical assistance.
2. MG mechanism is closely monitored quarterly and evaluated annually. The MG is modified in a timely way to take account of ongoing lessons of experience.
3. By the end of the project, a refined MG is available for replication and eventual "mainstreaming" within the Government's institutional and fiscal framework.

