

CONFORMED COPY

LOAN NUMBER 4310-BR

Project Agreement

(Federal Water Resources Management Project)

between

INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT

and

STATE OF PERNAMBUCO

Dated June 3, 1998

LOAN NUMBER 4310-BR

PROJECT AGREEMENT

AGREEMENT, dated June 3, 1998, between INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT (the Bank) and the STATE OF PERNAMBUCO (PERNAMBUCO);

WHEREAS (A) by the Loan Agreement of even date herewith between Federative Republic of Brazil (the Borrower) and the Bank, the Bank has agreed to make available to the Borrower an amount in various currencies equivalent to one hundred ninety eight million dollars (\$198,000,000), on the terms and conditions set forth in the Loan Agreement, but only on condition that PERNAMBUCO agree to undertake such obligations toward the Bank as are set forth in this Agreement;

(B) by an Institutional Development Agreement and one or more Subproject Agreements to be entered into between the Borrower and PERNAMBUCO, a portion of the proceeds of the loan provided for under the Loan Agreement will be transferred to PERNAMBUCO on the terms and conditions set forth in said agreements; and

WHEREAS PERNAMBUCO, in consideration of the Bank's entering into the Loan Agreement with the Borrower, has agreed to undertake the obligations set forth in this Agreement;

NOW THEREFORE the parties hereto hereby agree as follows:

ARTICLE I

Definitions

Section 1.01. Unless the context otherwise requires, the several terms defined in the preamble to this Agreement, the Loan Agreement and the General Conditions (as

so defined) have the respective meanings therein set forth.

ARTICLE II

Execution of the Project

Section 2.01. PERNAMBUCO declares its commitment to the objectives of the Project as set forth in Schedule 2 to the Loan Agreement, and, to this end, shall, through UEGP, carry out its corresponding activities under Parts A.2, B and D.2 of the Project, all with due diligence and efficiency and in conformity with: (i) the Institutional Development Agreement or the relevant Subproject Agreement, as applicable; (ii) the Operational Manual; (iii) the relevant State Annual Operating Plan; (iv) the State Implementation Plan; and (v) appropriate administrative, financial, engineering, environmental and land management practices; and shall provide, or cause to be provided, promptly as needed, the funds, facilities, services and other resources required for the carrying out of its corresponding activities under Parts A.2, B and D.2 of the Project.

Section 2.02. Except as the Bank shall otherwise agree, procurement of the goods, works and consultants' services required for the Project and to be financed out of the proceeds of the Loan shall be governed by the provisions of Schedule 4 to the Loan Agreement.

Section 2.03. PERNAMBUCO shall carry out the obligations set forth in Sections 9.04, 9.05, 9.06, 9.07 (a) and (b), 9.08 and 9.09 of the General Conditions (relating to insurance, use of goods and services, plans and schedules, records and reports, maintenance and land acquisition, respectively) in respect of its corresponding activities under Parts A.2, B and D.2 of the Project.

Section 2.04. PERNAMBUCO shall maintain, during Project implementation, with adequate facilities and equipment, a management unit (the UEGP) housed within PERNAMBUCO's Secretariat of Science, Technology and Environment with staff in adequate numbers and with adequate qualifications, and with responsibilities, structure and functions satisfactory to the Bank, including, the responsibility for the overall coordination and monitoring of PERNAMBUCO's participation in the implementation of Parts A.2, B and D.2 of the Project.

Section 2.05. Without limitation to the generality of Section 2.01 (a) of this Agreement and whenever a Subproject includes the construction of a dam which is fifteen meters or more in height, or which is between ten and fifteen meters in height and presents, in the reasonable opinion of the Bank, special design complexities, PERNAMBUCO shall: (A) establish and thereafter maintain during the design and initial operation of such Subproject, a Dam Safety Review Panel under terms of reference and arrangements acceptable to the Bank; (B) cause the relevant dam, reservoir and related structures to be periodically inspected by independent qualified professionals under terms of reference acceptable to the Bank, in order to determine whether there are any deficiencies in the condition of such structures, or in the quality and adequacy of maintenance or methods of operation of the same, which may endanger their safety; (C) furnish to the Bank for its review the periodic reports of the Dam Safety Review Panel (to be issued in accordance with its terms of reference) and of the professionals referred to in subparagraph (B) above, together with PERNAMBUCO's own comments; and (D) no later than six months before the expected completion of the relevant dam, reservoir and related structures, propose to the Bank for its review and approval, appropriate arrangements for their operation and maintenance.

Section 2.06. (a) Whenever a Subproject requires the undertaking of environmental protection measures and/or resettlement of population pursuant to Section 3.02 (b) (viii) of the Loan Agreement, PERNAMBUCO shall carry out the mitigation measures provided in the corresponding environmental assessment and/or carry out the resettlement action plan in a manner and within a timetable satisfactory to the Bank; (b) Whenever a Subproject requires the undertaking of measures to ensure the development and protection of indigenous peoples pursuant to Section 3.02 (b) (ix) of the Loan Agreement, PERNAMBUCO shall carry out the IPDP in a manner and within a timetable satisfactory to the Bank.

Section 2.07. PERNAMBUCO shall, in the month of October of each year during

Project implementation, furnish to SRH/MMA an annual plan (a State Annual Operating Plan), describing, inter alia, the Project activities to be carried out during the next calendar year, including the costs thereof.

Section 2.08. Without limitation upon the provisions of Section 9.01 (a) and 9.07 of the General Conditions, PERNAMBUCO shall:

(a) Beginning two months after the date of this Agreement, during each year of Project implementation furnish to the SRH/MMA quarterly reports on the progress in the implementation of PERNAMBUCO's activities under Parts A.2, B and D.2 of the Project during the previous three months which shall be based on the targets and indicators set forth in the State Implementation Plan and in the Project Monitoring Letter, respectively, such reports to be of such scope and in such detail as the Bank shall reasonably request; and

(b) in the months of March and September of each year during Project implementation hold reviews jointly with the Borrower and the Bank (the review to take place in the eighteenth month after the date of this Agreement or when disbursements from the Loan Account have reached 40% of the amount of the Loan, whichever is earlier, to be the mid-term review), such reviews to be based on the reports referred to in paragraph (a) above and, thereafter, take or cause to be taken all such action which shall have been agreed upon by PERNAMBUCO, the Borrower and the Bank during the reviews referred to in this paragraph, as necessary for the efficient execution of its corresponding activities under the Project or the achievement of its objectives, such action to be taken in the manner and within the timetable agreed upon during such reviews.

Section 2.09. PERNAMBUCO shall carry out the plan referred to in Section 3.02 (b) (iii) of the Loan Agreement in accordance with its own terms, including the timetable set forth therein.

Section 2.10. PERNAMBUCO shall assist the Borrower in the preparation of the plan referred to in Section 3.06 of the Loan Agreement and the report referred to in Section 9.07 (c) of the General Conditions.

Section 2.11. PERNAMBUCO shall exercise its rights and comply with its obligations under its respective Institutional Development Agreement and under each Subproject Agreement in such a manner as to protect the interests of the Borrower and the Bank, and, except as the Bank shall otherwise agree, PERNAMBUCO shall not amend, suspend, abrogate, waive or fail to enforce the Institutional Development Agreement or each Subproject Agreement, or any provision thereof.

Section 2.12. PERNAMBUCO shall promptly inform the Bank and the Borrower of any condition which interferes or threatens to interfere with the progress in the carrying out of its activities under the Project, the accomplishment of the purposes of the Loan, or the performance by PERNAMBUCO of its obligations under this Agreement, the Institutional Development Agreement and under each Subproject Agreement.

ARTICLE III

Financial Covenants

Section 3.01 (a) PERNAMBUCO shall maintain records and separate accounts adequate to reflect in accordance with sound accounting practices the operations, resources and expenditures, in respect of its activities under Parts A.2, B and D.2 of the Project, of the departments or agencies of PERNAMBUCO responsible for the carrying out of such activities.

(b) PERNAMBUCO shall:

(i) have the records and accounts referred to in paragraph (a) above for each auditing principles auditors acceptable to the Bank; fiscal year audited, in accordance with appropriate consistently applied, by independent

(ii) furnish to the Bank 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 Bank shall have reasonably requested; and

(iii) furnish to the Bank such other information concerning said records
and accounts, and the audit thereof, as the Bank shall from time
to time reasonably request.

ARTICLE IV

Effective Date; Termination; Cancellation and Suspension

Section 4.01. This Agreement shall come into force and effect on the date upon
which the Loan Agreement becomes effective.

Section 4.02. This Agreement and all obligations of the Bank and of PERNAMBUCO
thereunder shall terminate on the date on which the Loan Agreement shall terminate in
accordance with its terms, and the Bank shall promptly notify PERNAMBUCO thereof.

Section 4.03. All the provisions of this Agreement shall continue in full force
and effect notwithstanding any cancellation or suspension under the General
Conditions.

ARTICLE V

Miscellaneous Provisions

Section 5.01. Any notice or request required or permitted to be given or made
under this Agreement and any agreement between the parties contemplated by this
Agreement shall be in writing. Such notice or request shall be deemed to have been
duly given or made when it shall be delivered by hand or by mail, telegram, cable,
telex or radiogram to the party to which it is required or permitted to be given or
made at such party's address hereinafter specified or at such other address as such
party shall have designated by notice to the party giving such notice or making such
request. The addresses so specified are:

For the Bank:

International Bank for
Reconstruction and Development
1818 H Street, N.W.
Washington, D.C. 20433
United States of America

Cable address:

INTBAFRAD
Washington, D.C.

Telex:

248423 (MCI) or
64145 (MCI)

For PERNAMBUCO:

Secretaria de Ciência, Tecnologia e Meio Ambiente
do Estado de Pernambuco
Rua Irmã Maria David, 180 Casa Forte
52061-070, Recife, Pernambuco
Brazil

With copies to:

Ministério do Planejamento e Orçamento
Secretaria de Assuntos Internacionais
Esplanada dos Ministérios, Bloco "K" - 5º andar
70040-906, Brasília, D.F.
Brazil

Ministério do Meio Ambiente,

Recursos Hídricos e Amazônia Legal
Secretaria de Recursos Hídricos
SGAN Quadra 601, Lote 1, 4º andar
70830-901, Brasília - D.F.
Brazil

Section 5.02. Any action required or permitted to be taken, and any document required or permitted to be executed, under this Agreement on behalf of PERNAMBUCO may be taken or executed by the Governor of PERNAMBUCO or such other person or persons as such Governor shall designate in writing, and PERNAMBUCO shall furnish to the Bank sufficient evidence of the authority and the authenticated specimen signature of each such person.

Section 5.03. This Agreement may be executed in several counterparts, each of which shall be an original, and all collectively but one instrument.

IN WITNESS WHEREOF, the parties hereto, acting through their duly authorized representatives, have caused this Agreement to be signed in their respective names in Brasilia, D.F., Brazil, as of the day and year first above written.

INTERNATIONAL BANK FOR
RECONSTRUCTION AND DEVELOPMENT

By /s/ Robert Schneider

Authorized Representative

STATE OF PERNAMBUCO

By /s/ Sérgio Machado Rezende

Authorized Representative

