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CONFORMED COPY

LOAN NUMBER 4614-PE

Loan Agreement

(Second Rural Roads Project)

between

REPUBLIC OF PERU

and

INTERNATIONAL BANK FOR RECONSTRUCTION

AND DEVELOPMENT

Dated June 26, 2001

LOAN NUMBER 4614-PE

LOAN AGREEMENT

AGREEMENT, dated June 26, 2001 between REPUBLIC OF PERU (the Borrower) and INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT (the Bank).

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

(B)

on August 6, 1984 the Borrower's Congress passed Law No. 23853 (the Municipal Organic Law) that requires Provincial Municipalities and District Municipalities (both as hereinafter defined) to maintain the Borrower's rural roads network;

(C)

on July 10, 1999 the Borrower's Congress passed Law No. 27181 (the Transport Law) that requires the Borrower's Ministry of Transport, Communications, Housing and Construction (MTC) to support Provincial Municipalities and District Municipalities (both as hereinafter defined) in the maintenance of the Borrower's rural roads network;

(D)

on June 19, 1995, the Borrower issued Supreme Decree No. 09-95-MTC (Supreme Decree No. 09-95-MTC) that establishes the categories of roads within the Borrower's road network;

(E)

on October 19, 2000, the Provincial Municipality (as hereinafter defined) of Arequipa issued Ordinance No. 46 (Ordinance No. 46) that established Instituto de Vialidad Municipal de la Provincia de Arequipa (IVP) as a decentralized public entity, with legal personality, and administrative, economic, budget and financial autonomy;

(F)

the Borrower intends to contract from the Inter-American Development Bank (IDB) a loan (the IDB Loan) in an amount equivalent to fifty million dollars (\$50,000,000) to assist in financing the Project on the terms and conditions set forth in an agreement (the IDB Loan Agreement) to be entered into between the Borrower and

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IDB;

WHEREAS the Bank has agreed, on the basis, inter alia, of the foregoing, to extend the Loan 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 Loan and Guarantee Agreements for Single Currency Loans" of the Bank, dated May 30, 1995 (as amended through October 6, 1999) (the General Conditions) constitute an integral part of this Agreement.

Section 1.02. Unless the context otherwise requires, the several terms defined in the General Conditions and in the Preamble to this Agreement have the respective

meanings therein set forth and the following additional terms have the following meanings:

(a)

"Annual Investment Program" means any of the programs referred to in Section 3.10 (a) (i) of this Agreement;

(b)

"Community" means any rural community living in the Project Area (as hereinafter defined);

(c)

"Community-based Micro-enterprise" means any Community-based micro enterprise referred to in Section 3.04 (a) (i) (A) of this Agreement;

(d)

"Connecting Primary Road" means any road in the Project Area (as hereinafter defined) classified as Ruta Nacional pursuant to Article 1 of Supreme Decree No. 09-95-MTC that is directly connected with, and provides access to, a Rural Road (as hereinafter defined);

(e)

"Connecting Secondary Road" means any road in the Project Area classified as Ruta Departamental pursuant to Article 1 of Supreme Decree No. 09-95-MTC that is directly connected with, and provides access to, a Rural Road (as hereinafter defined);

(f)

"District Municipality" means Municipalidad Distrital, any of the political subdivisions of a Provincial Municipality (as hereinafter defined) established pursuant to paragraph 3 of Article 4 of the Municipal Organic Law;

(g)

"Eligible Categories" means categories (1) through (5) set forth in the table in Part A.1 of Schedule 1 to this Agreement;

(h)

"Eligible Expenditures" means the expenditures for works and services referred to in Section 2.02 of this Agreement;

(i)

"Environmental and Indigenous Peoples' Guidelines" means the guidelines for the preparation of the environmental impact assessment and the indigenous peoples development plan for Parts E.2, E.3 and E.4 of the Project set forth in the letter from the Borrower to the Bank dated May 28, 2001;

(j)

"FCM" means Fondo de Compensación Municipal, the Borrower's municipal compensation fund established under the Borrower's Legislative Decree No. 776;

(k)

"First Project" means the Rural Roads Rehabilitation and Maintenance Project financed under the Loan Agreement entered into between the Borrower and the Bank on December 7, 1995 (Loan No. 3962-PE);

(l)

"Institutional Action Plan" means any of the action plans referred to in Section 3.05 (a) of this Agreement;

(m)

"Local Currency Account" means the account referred to in Section 3.15 (a) of this Agreement;

(n)

"MCM" means the maintenance cofinancing mechanism referred to in Section 3.09 (a) (vi);

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(o)

"Municipality" means any District Municipality or Provincial Municipality (as hereinafter defined);

(p)

"NGO" means any non-governmental organization (with legal personality) operating in the Project Area (as hereinafter defined);

(q)

"Non-Project Road" means any road in the Project Area (as hereinafter defined) that is not a Project Road (as hereinafter defined);

(r)

"Operational Manual" means the Project operational manual referred to in Section 3.09 (a) of this Agreement;

(s)

"Participation Agreement" means any of the agreements referred to in Section 3.04 of this Agreement;

(t)

"Partnership Agreement" means any of the agreements referred to in Section 3.07 of this Agreement;

(u)

"PCR" means Programa de Caminos Rurales, the central unit in MTC referred to in Section 3.03 (a) (ii) of this Agreement;

(v)

"Performance Indicators" means the Project performance indicators set forth in the letter from the Borrower to the Bank of even date herewith (Supplemental Letter);

(w)

"Project Area" means the area comprised by the Provincial Municipalities (as hereinafter defined) of the Borrower's departments of Ancash, Apurimac, Ayacucho, Cajamarca, Cusco, Huancavelica, Huanuco, Junín, Pasco, Puno, Madre de Dios and San Martín, the Provincial Municipality of Arequipa (in respect of Part D of the Project), the District Municipalities of Masisea, Tahuania and Campoverde in the Provincial Municipalities of Coronel Portillo and Atalaya (in respect of Part E of the Project), and any other Provincial Municipality which may be acceptable to the Bank in addition to, or in substitution of, the above Provincial Municipalities (as hereinafter defined);

(x)

"Project Management Report" means each report prepared in accordance with Section 4.02 of this Agreement;

(y)

"Project Road" means any Connecting Primary Road, Connecting Secondary Road, Rural Road or Unclassified Road (both as hereinafter defined) to be rehabilitated or maintained under the Project;

(z)

"Provincial Municipality" means Municipalidad Provincial, any of the political subdivisions of the Project Area established pursuant to paragraph 2 of Article 4 of the Municipal Organic Law;

(aa)

"Rural Road" means any road in the Project Area classified as Ruta Vecinal pursuant to Article 1 of Supreme Decree No. 09-95-MTC;

(bb)

"Rural Roads Committee" means any of the committees referred to in Section 3.04 (a) (i) (B) of this Agreement;

(cc)

"Special Account" means the account referred to in Part B.1 of Schedule 1 to this Agreement;

(dd)

"Steering Committee" means the Project steering committee referred to in Section 3.03 (a) (i) of this Agreement;

(ee)

"Subproject" means any of the investment subprojects referred to in Section 3.05 (b) of this Agreement;
(ff)

"Unclassified Road" means any non-motorized track or footpath in villages or small towns in the Project Area which is directly connected with, and provides access to, Rural Roads; and
(gg)

"UZ" means any of the zonal units of PCR referred to in Section 3.03 (a) (iii) of this Agreement.

ARTICLE II

The Loan

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Section 2.01. The Bank agrees to lend to the Borrower, on the terms and conditions set forth or referred to in this Agreement, an amount equal to fifty million Dollars (\$50,000,000).

Section 2.02. The amount of the Loan may be withdrawn from the Loan Account in accordance with the provisions of Schedule 1 to this Agreement for expenditures made (or, if the Bank shall so agree, to be made) in respect of the reasonable cost of works and services required for the Project described in Schedule 2 to this Agreement and to be financed out of the proceeds of the Loan, and in respect of the front-end fee referred to in Section 2.04 of this Agreement.

Section 2.03. The Closing Date shall be June 30, 2005 or such later date as the Bank shall establish. The Bank shall promptly notify the Borrower of such later date.

Section 2.04. The Borrower shall pay to the Bank a fee in an amount equal to one percent (1%) of the amount of the Loan. On or promptly after the Effective Date, the Bank shall, on behalf of the Borrower, withdraw from the Loan Account and pay to itself the amount of said fee.

Section 2.05. The Borrower shall pay to the Bank a commitment charge at the rate of three-fourths of one percent ($3/4$ of 1%) per annum on the principal amount of the Loan not withdrawn from time to time.

Section 2.06. (a) The Borrower shall pay interest on the principal amount of the Loan withdrawn and outstanding from time to time, at a rate for each Interest Period equal to LIBOR Base Rate plus LIBOR Total Spread.

(b)

For the purposes of this Section:

(i)

"Interest Period" means the initial period from and including the date of this Agreement to, but excluding, the first Interest Payment Date occurring thereafter, and after the initial period, each period from and including an Interest Payment Date to, but excluding the next following Interest Payment Date.

(ii)

"Interest Payment Date" means any date specified in Section 2.07 of this Agreement.

(iii)

"LIBOR Base Rate" means, for each Interest Period, the London interbank offered rate for six-month deposits in Dollars for value the first day of such Interest Period (or, in the case of the initial Interest Period, for value the Interest Payment Date occurring on or next preceding the first day of such Interest Period), as reasonably determined by the Bank and expressed as a percentage per annum.

(iv)

"LIBOR Total Spread" means, for each Interest Period: (A) three-fourths of one percent ($3/4$ of 1%); (B) minus (or plus) the weighted average margin, for such Interest Period, below (or

above) the London interbank offered rates, or other reference rates, for six-month deposits, in respect of the Bank's outstanding borrowings or portions thereof allocated by the Bank to fund single currency loans or portions thereof made by it that include the Loan; as reasonably determined by the Bank and expressed as a percentage per annum.

(c)

The Bank shall notify the Borrower of LIBOR Base Rate and LIBOR Total Spread for each Interest Period, promptly upon the determination thereof.

(d)

Whenever, in light of changes in market practice affecting the determination of the interest rates referred to in this Section, the Bank determines that it is in the interest of its borrowers as a whole and of the Bank to apply a basis for determining the interest rates applicable to the Loan other than as provided in said Section, the Bank may modify the basis for determining the interest rates applicable to the Loan upon not less than six (6) months' notice to the Borrower of the new basis. The basis shall become effective on the expiry of the notice period unless the Borrower notifies the Bank during said period of its objection thereto, in Page 5

which case said modification shall not apply to the Loan.

Section 2.07. Interest and other charges shall be payable semiannually in arrears on February 15 and August 15 in each year.

Section 2.08. The Borrower shall repay the principal amount of the Loan in accordance with the amortization schedule set forth in Schedule 3 to this Agreement.

ARTICLE III

Execution of the Project

Section 3.01. The Borrower declares its commitment to the objectives of the Project as set forth in Schedule 2 to this Agreement, and, to this end, shall carry out the Project, through MTC, with due diligence and efficiency and in conformity with appropriate engineering, managerial, technical, financial, social and environmental practices, and shall provide, promptly as needed, the funds, facilities, services and other resources required for the Project.

Section 3.02. Except as the Bank shall otherwise agree, procurement of the 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 this Agreement.

Section 3.03. (a) At all times during the execution of the Project, the Borrower (through MTC) shall maintain:

(i)

a Project steering committee with membership structure and responsibilities satisfactory to the Bank, including the following responsibilities: (A) to review Project implementation reports and audits; and (B) to approve the Operational Manual, each Annual Investment Program, and any modification thereof;

(ii)

a central unit in MTC responsible for overall Project management, including: (A) entering into Participation Agreements and Partnership Agreements; (B) preparing Annual Investment Programs; (C) coordinating Project interventions with other agencies of the Borrower and civil society representatives at the national level; (D) issuing Project implementation guidelines; (E) channeling the proceeds of the Loan in a manner consistent with the MCM; (F) upkeeping the Project impact monitoring system; (G) auditing the performance of UZs; (H) procuring works and consultants' services for the Project; and (I) preparing Project Management Reports and processing withdrawal applications; and

(iii)
zonal units of PCR in the Project Area, responsible for managing Project implementation in the Project Area, including: (A) coordinating Project interventions with other agencies of the Borrower and civil society representatives at the departmental level; (B) preparing proposals for inclusion in the Annual Investment Programs in consultation with Municipalities; and (C) monitoring and reporting of Project implementation.

(b)
The Borrower, through MTC, shall ensure that PCR and UZs are staffed, at all times during the execution of the Project, by professional staff in numbers and with experience and qualifications acceptable to the Bank, operating under terms of reference satisfactory to the Bank, all as prescribed in the Operational Manual. Section 3.04. The Borrower, through PCR, shall enter into agreements with Provincial Municipalities (with the consent of all District Municipalities within the jurisdiction of the respective Provincial Municipality), under terms and conditions satisfactory to the Bank, for the purposes of ensuring the participation of such Municipalities in the implementation of the Project, such agreements to provide:

(a)
the following obligations of the Municipalities:

(i)
to support the development of: (A) community-based
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micro-enterprises capable to carry out civil works for Rural Roads rehabilitation and maintenance; and (B) community committees to support Unclassified Roads rehabilitation and maintenance;

(ii)
to establish the financial arrangements required to support the flow of funds for Rural Roads maintenance under the MCM; and

(iii)
to make budgetary allocations and release the funds to maintain Project Roads on a timely basis;

(b)
the following obligations of PCR:

(i)
to inform the Municipalities about Project-financed activities;

(ii)
to provide technical assistance to the Municipalities for their institutional strengthening in Rural Roads management;

(iii)
to evaluate jointly with the Municipalities the results of Project activities; and

(iv)
to establish a financial mechanism to allow Municipalities to continue funding maintenance of Rural Roads rehabilitated under the Project and channel the Borrower's contributions as required under the MCM; and

(c)
the close coordination between the Municipalities and the respective UZ for the selection of Project Roads, the identification and evaluation of Subprojects, and the execution of the works and services contracts under such Subprojects, as prescribed in the Operational Manual.

Section 3.05. Pursuant to the Participation Agreements, the parties to such Agreements shall:

(a)

develop and implement action plans, satisfactory to the Bank, for purposes of strengthening the capacity of the respective Municipalities to manage their Rural Roads network and improve the condition of transport services within their jurisdictions, including the preparation of transport plans and road inventories, and the exchange of information on the overall performance of such Municipalities' rural roads system; and

(b)

select investment subprojects for the financing of rehabilitation or maintenance of Project Roads, or sections thereof, to ensure adequate transitivity and access, all in accordance with the criteria and standards set forth in the Operational Manual, such subprojects to be included in an Annual Investment Program. Section 3.06. (a) Prior to the approval of any proposed Subproject, the Borrower, through PCR, shall apply the environmental assessment procedures and guidelines prescribed in the Operational Manual, in order to:

(i)

carry out an environmental screening and assessment of such proposed Subproject; and

(ii)

prepare recommendations for prevention, mitigation and remediation of any potential environmental damage arising from the implementation of such proposed Subproject.

(b)

During the implementation of any Subproject, the Borrower, through PCR, shall ensure that UZs and the Municipalities carry out the recommendations of the environmental assessment as prescribed in the Operational Manual.

Section 3.07. With respect to Part C.2 of the Project, the Borrower (through PCR) shall enter into agreements with Rural Roads Committees (on behalf of Communities), under terms and conditions satisfactory to the Bank, for the purposes of ensuring the participation of such Communities in the implementation of such Part of

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the Project by:

(a)

identifying Subprojects and recommending solutions for improving transport services in Unclassified Roads;

(b)

contributing to the cost of the works financed under such Part of the Project;

(c)

establishing Community-based committees to undertake the improvement of Unclassified Roads;

(d)

undertaking related local development initiatives; and

(e)

joining PCR and UZs in monitoring and evaluating Project impact.

Section 3.08. (a) The Borrower, through PCR, shall exercise its rights and carry out its obligations under each Participation Agreement and each Partnership Agreement in such a manner as to protect the interests of the Borrower and the Bank and to accomplish the purposes of the Loan and, except as the Bank shall otherwise agree, the Borrower shall not assign, amend, abrogate, waive or fail to enforce any Participation Agreement or any Partnership Agreement or any provision thereof.

(b)

Without limitation or restriction to any of the Bank's rights under this Agreement, in the event that any Provincial Municipality fails to perform any of its obligations under the applicable Participation Agreement to the satisfaction of the Bank, the Borrower, through PCR, shall:

(i)

not include in any proposed Annual Investment Program activities (including Subprojects) within the jurisdiction, or for the benefit, of such Provincial Municipality until such Provincial Municipality has taken corrective action to the satisfaction of PCR and the Bank; and

(ii)

exclude from the Annual Investment Program activities (including Subprojects) within the jurisdiction, or for the benefit, of such Provincial Municipality, other than the activities for which the contracting of works or services has been finalized pursuant to the provisions of Schedule 4 to this Agreement.

Section 3.09. (a) The Borrower, through MTC, shall carry out the Project in accordance with an operational manual, satisfactory to the Bank, said manual to provide the rules and procedures for the implementation of the Project, in the areas of:

(i)

Project institutional setup, including organization and functions of PCR and UZs;

(ii)

disbursement, accounting, auditing and reporting procedures;

(iii)

procurement responsibilities, processes and internal controls;

(iv)

monitoring and evaluation plans for the Project;

(v)

procedures for identification, preparation, approval, execution and supervision of Subprojects, including environmental assessment procedures and guidelines, and a list of non-eligible works; and

(vi)

a Rural Road cofinancing mechanism for PCR and Municipalities.

(b)

If any provision of the Operational Manual is inconsistent with a provision of this Agreement, the provisions of this Agreement shall govern.

Section 3.10. (a) The Borrower, through PCR, shall:

(i)

not later than November 30 of each year of Project implementation, starting in November 30, 2001, furnish to the Bank, for its review, an annual investment program for the following calendar

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year, such program to specify: (A) the activities (including Subprojects) to be financed out of the proceeds of the Loan during the respective calendar year in the Project Area; (B) the implementation schedule and MTC's budget proposal for such activities; and (C) information on the rehabilitation and maintenance activities that MTC intends to undertake in the Project Area with its own resources in Non-Project Roads that are critical because of their integration with Project Roads; and

(ii)

upon the Bank's approval, carry out such Annual Investment Program in accordance with its terms.

(b)

The Bank may refrain from approving any Annual Investment Program if the Bank has determined that the Borrower is not carrying out the Project as provided in this Agreement and no appropriate remedial actions, satisfactory to the Bank, have been taken therefor.

Section 3.11. The Borrower, through PCR, shall:

- (a) maintain policies and procedures adequate to enable it to monitor and evaluate on an ongoing basis, in accordance with the Performance Indicators, the carrying out of the Project and the achievement of the objectives thereof; and
- (b) not later than January 31, April 30, July 31 and October 31 of each year of Project implementation, starting in October 31, 2001, furnish to the Bank progress reports on the execution of the Project during the preceding calendar quarter, of such scope and in such detail as the Bank may reasonably request, including, inter alia:
 - (i) information on the progress achieved during the previous calendar quarter in the carrying out of the Project and the achievement of the objectives thereof;
 - (ii) an assessment of the issues and options arising from Project implementation;
 - (iii) updated implementation and disbursement schedules for the ongoing calendar quarter; and
 - (iv) compliance of Borrower's obligations under this Agreement and, whenever necessary, action plans proposed to ensure such compliance.

Section 3.12. The Borrower, through PCR, shall:

- (a) not later than November 30 of each year of Project implementation, starting in November 30, 2001, hold a Project annual review with the Bank, such review to be based on the reports referred to in Section 3.11 (b) of this Agreement and to focus, inter alia, on:
 - (i) progress in the execution of the Project and the achievement of its objectives during the previous year;
 - (ii) performance of PCR and UZs;
 - (iii) effectiveness of the Annual Investment Programs in terms of Communities and Municipalities involvement, local contractors response and coordination with other rural development programs in the Project Area;
 - (iv) progress in the implementation of Part F of the Project, including compliance of the Municipalities with the Institutional Action Plans;
 - (v) experience with the rules and procedures set forth in the Operational Manual;
 - (vi) progress in restructuring and strengthening the overall administration and financing of Rural Roads maintenance; and
 - (vii) justification of the investment and institutional proposals for the implementation of the Project during the subsequent year;

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- (b) in respect of the annual review to be held not later than November 30, 2003, focus on the following matters in addition to those mentioned in paragraph (a)

above:

- (i) progress in the Borrower's administrative decentralization within the rural roads sector and possible adjustments to Project operational setup;
 - (ii) adoption of a strategy for rural roads sector funding;
 - (iii) improvement of the Borrower's inter-agency coordination in the rural roads sector; and
 - (iv) evaluation of the implementation of Parts D and E of the Project;
- and

(c) if, as a result of any of the above reviews, the Bank shall have reasonably determined that the progress in the execution of the Project or in the achievement of its objectives is not satisfactory, promptly take or cause to be taken all such remedial action, satisfactory to the Bank, as shall be necessary for the efficient execution of the Project or the timely achievement of its objectives.

Section 3.13. The Borrower, through PCR, shall:

(a) not later than December 31, 2001 of Project implementation, contract technical audits for each semester of Project implementation, with independent auditors of experience and qualifications satisfactory to the Bank operating under terms of reference satisfactory to the Bank, such audits to focus on the performance of PCR and UZs in the implementation of the Project, including achievement of physical targets, quality and cost of the works, and compliance with the eligibility criteria, procurement, disbursement and environmental procedures set forth in the Operational Manual;

(b) not later than March 31 and September 30 of each year of Project implementation, furnish to the Bank the report of such audits by said auditors; and

(c) not later than May 31 and November 30 of each year of Project implementation, discuss the results of such audits with representatives of Municipalities and Communities involved in Project activities, taking into account the Bank's comments thereon.

Section 3.14. The Borrower, through PCR, shall:

(a) not later than June 30, 2003, contract an impact evaluation study with independent consultants of experience and qualifications satisfactory to the Bank, operating under terms of reference satisfactory to the Bank, such study to assess overall Project economic, social and environmental impact;

(b) not later than October 31, 2003, furnish to the Bank, for its review and comments, the findings and recommendations of such study by said consultants; and

(c) not later than November 30, 2003, review with Communities, Municipalities and NGOs involved in Project activities, as well as other agencies of the Borrower involved in rural development programs, the results of such impact evaluation study taking into account the Bank's comments thereon.

Section 3.15. The Borrower, through PCR, shall:

(a) open and maintain a local currency account, in a commercial bank acceptable to the Bank under terms and conditions satisfactory to the Bank; and

(b)

deposit in such Local Currency Account, at the beginning of each month during the execution of the Project, the counterpart funding required for payments to be made during that month in respect of expenditures on account of works or services procured or to be procured under the Project.

Section 3.16. With regard to Part D of the Project:

(a)

the Borrower (through PCR) shall ensure that the Participation Agreement with the Provincial Municipality of Arequipa shall provide terms and conditions,

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satisfactory to the Bank, for the implementation of such Part of the Project by IVP; and

(b)

subject to the Bank's prior approval, the Borrower (through PCR) shall include in the Participation Agreements with other Provincial Municipalities that meet the eligibility requirements for the implementation of such Part of the Project provided in the Operational Manual terms and conditions similar to the ones referred to in paragraph (a) above.

Section 3.17. With regard to Part E of the Project, the Borrower (through PCR):

(a)

(i)

not later than October 31, 2002, shall complete the implementation of Parts E.1 and E.5 of the Project;

(ii)

not later than November 30, 2002, shall start the implementation of Part E.6 of the Project; and

(iii)

not earlier than February 28, 2003, shall commence the procurement of the works required for the implementation of Parts E.2, E.3 and E.4 of the Project,

all in accordance with a timetable satisfactory to the Bank, and with the assistance of economic, social and environmental experts of experience and qualifications acceptable to the Bank, operating under terms of reference satisfactory to the Bank; and

(b)

shall refrain from commencing the implementation of Parts E.2, E.3 and E.4 of the Project, irrespective of the source of financing, until the Bank has confirmed its satisfaction with the environmental impact assessments and indigenous peoples development plans referred to in paragraph 3 (c) (ii) of Part A of Schedule 1 to this Agreement.

Section 3.18. For the purposes of Section 9.07 of the General Conditions and without limitation thereto, the Borrower (through PCR) shall:

(a)

prepare, on the basis of guidelines acceptable to the Bank, and furnish to the Bank not later than six (6) months after the Closing Date or such later date as may be agreed for this purpose between the Borrower and the Bank, a plan for the continued achievement of Project objectives; and

(b)

afford the Bank a reasonable opportunity to exchange views with the Borrower on said plan.

ARTICLE IV

Financial Covenants

Section 4.01. (a) The Borrower, through MTC, shall establish and thereafter maintain a financial management system, including records and accounts, and prepare financial statements in a format acceptable to the Bank, adequate to reflect the operations, resources and expenditures related to the Project.

(b)

The Borrower, through MTC, shall:

(i)

have the records, accounts and financial statements referred to in paragraph (a) of this Section and the records and accounts for the Special Account for each fiscal year audited, in accordance with auditing standards acceptable to the Bank, consistently applied, by independent auditors acceptable to the Bank;

(ii)

furnish to the Bank as soon as available, but in any case not later than four (4) months after the end of each such year: (A) certified copies of the financial statements referred to in paragraph (a) of this Section for such year as so audited; and (B) an opinion on such statements, records and accounts and report of such audit, by said auditors, of such scope and in such detail as the Bank shall have reasonably requested; and

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(iii)

furnish to the Bank such other information concerning such records and accounts, and the audit thereof, and concerning said auditors, as the Bank may from time to time reasonably request.

(c)

For all expenditures with respect to which withdrawals from the Loan Account were made on the basis of Project Management Reports or statements of expenditure, the Borrower (through MTC) 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 (1) year after the Bank has received the audit report for the fiscal year in which the last withdrawal from the Loan Account was made, all records (contracts, orders, invoices, bills, receipts and other documents) evidencing such expenditures;

(iii)

enable the Bank'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 (through MTC) shall carry out a time-bound action plan acceptable to the Bank for the strengthening of the financial management system referred to in paragraph (a) of Section 4.01 of this Agreement in order to enable the Borrower (through MTC) not later than April 30, 2002 or such later date as the Bank shall agree, to prepare quarterly Project management reports, acceptable to the Bank, each of which:

(i)

(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 Loan during the period covered by said report and expenditures proposed to be financed out of the proceeds of the Loan during the six-month period following the period covered by said report;

(ii)

(A) describes 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; and

(iii)

sets forth the status of procurement under the Project and expenditures under contracts financed out of the proceeds of the Loan, 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 (through MTC) shall prepare, in accordance with guidelines acceptable to the Bank, and furnish to the Bank not later than forty-five (45) days after the end of each calendar quarter a Project Management Report for such period.

ARTICLE V

Remedies of the Bank

Section 5.01. Pursuant to Section 6.02 (p) of the General Conditions, the following additional events are specified:

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(a)

that the Municipal Organic Law or the Transport Law or Supreme Decree No. 09-95-MTC or Ordinance No. 46 or any provision thereof shall have been amended, suspended, abrogated, repealed or waived so as to affect materially and adversely the ability of the Borrower to perform any of its obligations under this Agreement;

(b)

that the IDB Loan Agreement shall have failed to become effective by not later than December 31, 2001 or such later date as the Bank may agree; provided, however, that the provisions of this paragraph shall not apply if the Borrower establishes to the satisfaction of the Bank that adequate funds for the Project are available to the Borrower from other sources on terms and conditions consistent with the obligations of the Borrower under this Agreement; and

(c)

(i)

Subject to subparagraph (ii) of this paragraph:

(A)

the right of the Borrower to withdraw the proceeds of the IDB Loan shall have been suspended, cancelled or terminated in whole or in part, pursuant to the terms of the IDB Loan Agreement; or

(B)

the IDB Loan shall have become due and payable prior to the agreed maturity thereof.

(ii)

Subparagraph (i) of this paragraph shall not apply if the Borrower establishes to the satisfaction of the Bank that:

(A)

such suspension, cancellation, termination or prematuring is not caused by the failure of the Borrower to perform any of its obligations under the IDB Loan Agreement; and

(B)

adequate funds for the Project are available to the Borrower

from other sources on terms and conditions consistent with the obligations of the Borrower under this Agreement.

Section 5.02. Pursuant to Section 7.01 (k) of the General Conditions, the following additional events are specified:

(a)

that the event specified in paragraph (a) of Section 5.01 of this Agreement shall occur; and

(b)

that the event specified in paragraph (c) (i) (B) of Section 5.01 of this Agreement shall occur, subject to the proviso of paragraph (c) (ii) of that Section.

ARTICLE VI

Effective Date; Termination

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

(a)

that the Borrower shall have issued legislation, satisfactory to the Bank, that allow the Municipalities to utilize the transfers under FCM to meet their contributions under the MCM;

(b)

that PCR shall have entered into at least sixty-five (65) Participation Agreements with Provincial Municipalities that participated in the implementation of the First Rural Roads Rehabilitation and Maintenance Project;

(c)

that the Steering Committee shall have approved the Operational Manual; and

(d)

(i) that financial management arrangements, satisfactory to the Bank, shall have been established by PCR and become operational; and (ii) that the selection process of the independent auditors referred to in Section 4.01 (b) (i) of this Agreement shall have been started.

Section 6.02. The date September 24, 2001, is hereby specified for the purposes of Section 12.04 of the General Conditions.

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ARTICLE VII

Representative of the Borrower; Addresses

Section 7.01. The Minister of Economy and Finance of the Borrower 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:

Ministry of Economy and Finance

Jr. Junín 319

Lima, Peru

Facsimile:

(511) 4268500 or

(511) 4269822

For the Bank:

International Bank for

Reconstruction and Development

1818 H Street, N.W.

Washington, D.C. 20433

United States of America

Cable address:

Telex:

Facsimile:
INTBAFRAD
248423 (MCI)
(202) 477-6391
Washington, D.C.
64145 (MCI)

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

REPUBLIC OF PERU
By /s/ Javier Silva Ruete
Authorized Representative
INTERNATIONAL BANK FOR
RECONSTRUCTION AND DEVELOPMENT

By /s/ David de Ferranti
Regional Vice President
Latin America and the Caribbean

SCHEDULE 1
Withdrawal of the Proceeds of the Loan

Part A:
General

1.

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

Amount of the
Loan Allocated
% of

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(Expressed in Expenditures

Dollar

to be

Category

Equivalent)

Financed

(1)

Works under

32,170,000 50%

Parts A, B.2, B.3,

C, D and E

of the Project

(2)

Works under force

1,500,000 50%

account procedures

under Part B.3 of

Section 1 of Schedule 4

to this Agreement

(3)

Works under Part B.1

5,220,000 20% of

of the Project

expenditures

incurred prior to

December 31,

2002; and 15% thereafter
(4)
Consultants' 4,000,000 50%
services
related to: (i)
feasibility and
engineering
design studies,
and supervision
of works under
Parts A through E
of the Project; (ii)
technical and financial
audits referred to in
Section 3.13 of this
Agreement and in Section
4.01 (b) (i) of this
Agreement, respectively;
and (iii) impact evaluation
study referred to in
Section 3.14 of this
Agreement.

(5)
Consultants' services
3,320,000 50%
and training under
Part F of the Project

(6)
Fee
500,000
Amounts due
under
Section 2.04 of
this Agreement

(7)
Unallocated
3,290,000
TOTAL
50,000,000

2.

For purposes of this Schedule the term "training" means expenditures related to:
(i) training materials and rental of training facilities; and (ii) registration fees,
travel, and per diem of trainees.

3.

Notwithstanding the provisions of paragraph 1 above, no withdrawals shall be
made in respect of:

(a)

payments made for expenditures prior to the date of this Agreement,
except that withdrawals, in an aggregate amount not to exceed \$5,000,000, may be made
in respect of Categories (1) through (5) of the table set forth in Part A.1 of this
Schedule, on account of payments made for expenditures before that date but after
January 1, 2001;

(b)

payments made for expenditures in respect of Categories (1) through (4)

of the table set forth in Part A.1 of this Schedule, in respect of Project activities
Page 15

(including Subprojects) within the jurisdiction, or for the benefit, of a Municipality (other than any Municipality referred to in Section 6.02 (b) of this Agreement) unless such Municipality has entered into a Participation Agreement; and

(c)

payments made for expenditures under Category (1) of the table set forth in Part A.1 of this Schedule, for Parts E.2, E.3 and E.4 of the Project, unless PCR has: (i) completed the implementation of Parts E.1 and E.5 of the Project to the satisfaction of the Bank; (ii) furnished to the Bank the results of the specific environmental, social and economic assessments for Parts E.2, E.3 and E.4 of the Project, including an environmental impact assessment and an indigenous peoples development plan for related Subprojects (both satisfactory to the Bank) prepared in accordance with the Environmental and Indigenous Peoples' Guidelines; and (iii) furnished to the Bank a detailed framework for the implementation of Part E.6 of the Project, satisfactory to the Bank.

4.

The Bank may require withdrawals from the Loan Account to be made on the basis of statements of expenditure for expenditures for:

(a)

works under contracts not exceeding \$1,000,000 equivalent, excluding the first two contracts awarded under Part C.1 of Section I of Schedule 4 to this Agreement;

(b)

works under force account procedures under Part C.3 of Section I of Schedule 4 to this Agreement;

(c)

services provided by consulting firms under contracts not exceeding \$100,000;

(d)

services provided by individual consultants under contracts not exceeding \$50,000; and

(e)

training,

under such terms and conditions as the Bank shall specify by notice to the Borrower.

Part B:

Special Account

1.

The Borrower shall open and maintain in Dollars a special deposit account, in a commercial bank acceptable to the Bank, on terms and conditions satisfactory to the Bank, including appropriate protection against set-off, seizure and attachment.

2.

After the Bank has received evidence satisfactory to it that the Special Account has been opened, withdrawals from the Loan Account of amounts to be deposited into the Special Account shall be made as follows:

(a)

until the Bank 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 Bank 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.

Payments out of the Special Account shall be made exclusively for Eligible Expenditures. For each payment made by the Borrower out of the Special Account, the Borrower shall, at such time as the Bank shall reasonably request, furnish to the Bank such documents and other evidence showing that such payment was made exclusively for Eligible Expenditures.

4.

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

(a)

if the Bank determines at any time that any Project Management Report does not adequately provide the information required pursuant to Section 4.02 of this Agreement;

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(b)

if the Bank determines at any time that all further withdrawals should be made by the Borrower directly from the Loan Account; or

(c)

if the Borrower shall have failed to furnish to the Bank 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 Bank 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.

5.

The Bank 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 Bank 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 Loan Account pursuant to Section 6.02 of the General Conditions. Upon such notification, the Bank 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.

6.

(a)

If the Bank determines at any time that any payment out of the Special Account was made for an expenditure which is not an Eligible Expenditure, or was not justified by the evidence furnished to the Bank, the Borrower shall, promptly upon notice from the Bank, provide such additional evidence as the Bank may request, or deposit into the Special Account (or, if the Bank shall so request, refund to the Bank) an amount equal to the amount of such payment.

(b)

If the Bank 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 Bank, refund to the Bank such outstanding amount.

(c)

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

(d)

Refunds to the Bank made pursuant to subparagraphs (a), (b) or (c) of this paragraph 6 shall be credited to the Loan Account for subsequent withdrawal or for cancellation in accordance with the provisions of the Loan Agreement.

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 \$4,000,000 to be withdrawn from the Loan Account and deposited into the Special Account pursuant to paragraph 2 of this Annex; provided, however, that unless the Bank shall otherwise agree, the Authorized Allocation shall be limited to an amount equal to \$1,000,000 until the aggregate amount of withdrawals from the Loan Account, plus the total amount of all outstanding special commitments entered into by the Bank pursuant to Section 5.02 of the General Conditions shall equal or exceed \$5,000,000.

2.

Withdrawals of the Authorized Allocation and subsequent withdrawals to replenish the Special Account shall be made as follows:

(a)

For withdrawals of the Authorized Allocation, the Borrower shall furnish to the Bank 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 Bank shall, on behalf of the Borrower, withdraw from the Loan 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 Bank requests for deposit into the Special Account at such intervals as the Bank shall specify. Prior to or at the time of each such request, the Borrower shall furnish to the Bank 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

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replenishment is requested. On the basis of each such request, the Bank shall, on behalf of the Borrower, withdraw from the Loan Account and deposit into the Special Account such amount as the Borrower shall have requested and as shall have been shown by said 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 Bank from the Loan Account under one or more of the Eligible Categories.

3.

The Bank shall not be required to make further deposits into the Special Account, once the total unwithdrawn amount of the Loan minus the total amount of all outstanding special commitments entered into by the Bank pursuant to Section 5.02 of the General Conditions, shall equal the equivalent of twice the amount of the Authorized Allocation. Thereafter, withdrawal from the Loan Account of the remaining unwithdrawn amount of the Loan shall follow such procedures as the Bank shall specify by notice to the Borrower. Such further withdrawals shall be made only after and to the extent that the Bank 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 Bank may otherwise specify by notice to the Borrower, all withdrawals from the Loan Account shall be deposited by the Bank 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 Bank from the Loan Account under one or more of the Eligible Categories.

2.

Each application for withdrawal from the Loan 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 Loan, the Bank shall, on behalf of the Borrower, withdraw from the Loan Account and deposit into the respective Special Account an amount equal to the lesser of: (a) the amount so requested; and (b) the amount which the Bank 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 \$8,500,000.

The overall objective of the Project is to increase access of Communities to basic social services and income-generating activities, so as to alleviate rural poverty and raise living standards in the Project Area.

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

Part A:

Rehabilitation of Project Roads

Carrying out of Subprojects for the rehabilitation of: (a) about 3,225 kilometers of Rural Roads; and (b) about 350 kilometers of Connecting Primary Roads and Connecting Secondary Roads.

Part B:

Routine, Emergency and Periodic Maintenance of Project Roads

1.

Carrying out of Subprojects for the routine maintenance of Project Roads and roads rehabilitated under the First Project.

2.

Carrying out of Subprojects for emergency maintenance of Project Roads through contracts awarded to Community-based Micro-enterprises and other private contractors.

3.

Carrying out of Subprojects for periodic maintenance of Project Roads and roads rehabilitated under the First Project.

Part C:

Improvement of Non-Motorized Rural Transport

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1.

Provision of technical assistance for village-level infrastructure management aimed at ensuring that Communities will be determinant in the selection, planning, implementation and financing of Subprojects through Rural Road Committees.

2.

Carrying out of Subprojects for improving about 3,100 kilometers of Unclassified Roads through: (a) removing of unsafe spots and other impediments to non-motorized rural transport; and (b) constructing of appropriate facilities for non-motorized rural transport.

Part D:

Provincial Road Management Pilot

Carrying out of a provincial road management pilot, aimed at entrusting Provincial and District Municipalities with responsibilities for the management of a core road network through the financing of Subprojects for the rehabilitation and maintenance of Project Roads.

Part E:

River Transport Improvement Pilot

Carrying out of a river transport improvement pilot along the Ucayali river (between the cities of Pucallpa and Atalaya) aimed at improving rural accessibility in the Borrower's Amazonic region and enabling sustainable social and economic development in such region by:

1.

carrying out environmental, social and economic impact assessments and the corresponding engineering studies, including an indigenous peoples development plan;

2.

constructing of safe mooring and durable landing facilities to improve cargo handling, and passenger and worker's access;

3.

spot rehabilitation of existing Rural Roads connecting Communities to the improved landing facilities;

4.

rehabilitation of Unclassified Roads connecting landing facilities with Project Roads;

5.

design and implementation of a participatory monitoring and evaluation system to keep track of outcomes and medium term direct and indirect impacts; and

6.

establishment of partnerships among local authorities, other donors and civil society organizations for:

(a)

providing technical assistance and training in matters like land use planning, and marketing or commercialization strategies for local products;

(b)

strengthening local organizations to develop productive projects; and

(c)

promoting interventions in sectors such as water, sanitation, health and education.

Part F:

Institutional Development

1.

Improving Rural Transport Policy and Strategies at the Central Level

Provision of technical assistance and training to MTC in the areas of:

(a)

strengthening capacity to formulate a policy framework and strategy for rural transport consistent with the Borrower's decentralization and poverty reduction agendas;

(b)

conducting of a collaborative dialogue with other agencies of the Borrower on national priority cross-sectoral themes, including decentralization and poverty reduction;

(c)

coordinating investment programs with other agencies of the Borrower, including those in charge of poverty reduction;

(d)

monitoring Rural Roads performance, including rural transport services;

(e)

handling dialogue with Municipalities, strengthening community organizations and addressing gender issues; and

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(f)

widening contacts with civil society organizations and think tanks involved in rural development research activities.

2.

Improving Planning and Management of Rural Roads at the Local Level

Provision of technical assistance and training to Municipalities in the areas of:

(a)

managing the core rural road network under their jurisdiction through

organizational arrangements, planning and budgeting systems, and extensive use of labor-based methods and contract arrangements, including the preparation of provincial transport plans and road inventories;

(b)

carrying out and financing Rural Roads routine and periodic maintenance operations through demand-driven, flexible programs; and

(c)

involving users and other stakeholders in Rural Roads management so as to increase Municipalities' accountability, including participation of Communities in the rehabilitation and maintenance of Unclassified Roads.

3.

Developing Community-based Micro-enterprises for Rural Roads Maintenance

Provision of technical assistance and training to Communities in the areas of:

(a)

promoting the development of Community-based Micro-enterprises among local leaders;

(b)

assisting the constitution of such Community-based Micro-enterprises through legal and technical advice;

(c)

contracting out to Community-based Micro-enterprises maintenance of Rural Roads;

(d)

putting in place adequate contractual arrangements and payment systems for such Community-based Micro-enterprises;

(e)

developing the technical, organizational, financial and administrative capacity of Community-based Micro-enterprises;

(f)

supervising and monitoring maintenance works carried out by such Community-based Micro-enterprises; and

(g)

supporting a dissemination campaign among Municipalities on the benefits of Rural Roads maintenance by Community-based Micro-enterprises.

4.

Strengthening Rural Communities' and Households' Capacity

Establishment of a local development window consisting of a network of strategic partnerships among local authorities, other donors and civil society organizations with a concerted strategy to complement Project-financed activities with other development interventions, through the provision of technical assistance and training in the areas of:

(a)

strengthening relationships between Communities and networks of markets and institutions;

(b)

assisting Communities in identifying, structuring and financing local initiatives and productive undertakings;

(c)

empowering Communities by building up basic human and social capabilities needed to take a proactive role in initiating or expanding development activities; and

(d)

establishing private sector-led mechanisms for coordinating, channeling and monitoring specialized assistance.

* * *

The Project is expected to be completed by December 31, 2004

SCHEDULE 3

Amortization Schedule

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Payment of Principal

Date Payment Due

(Expressed in Dollars)*

On each February 15 and August 15

beginning February 15, 2007

through February 15, 2018

2,085,000

on August 15, 2018

2,045,000

*

The figures in this column represent the amount in Dollars to be repaid, except as provided in Section 4.04 (d) of the General Conditions.

SCHEDULE 4

Procurement

Section I.

Procurement of Works

Part A:

General

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 Bank in January 1995 and revised in January and August 1996, September 1997 and January 1999 (the Guidelines) and the following provisions of Sections I and III of this Schedule.

Part B:

International Competitive Bidding

Except as otherwise provided in Part C of this Section, 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.

Part C:

Other Procurement Procedures

1.

National Competitive Bidding

Works estimated to cost less than \$3,000,000 but more than \$50,000 equivalent per contract, and not exceeding in the aggregate \$60,000,000 equivalent, may be procured under contracts awarded in accordance with the provisions of paragraphs 3.3 and 3.4 of the Guidelines

2.

Direct Contracting

Works estimated to cost \$50,000 equivalent or less per contract, and not

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exceeding in the aggregate \$57,700,000 equivalent, may be procured under contracts awarded directly either to Rural Roads Committees or Community-based Micro-enterprises in accordance with criteria and procedures satisfactory to the Bank on the basis of standard regionalized unit prices satisfactory to the Bank, as prescribed in the Operational Manual.

3. Force

Account

Works for Parts B.2 and B.3 of the Project which: (a) meet the requirements of paragraph 3.8 of the Guidelines; (b) cost \$50,000 equivalent or less per contract, not exceeding in the aggregate \$3,000,000 equivalent; and (c) are of equipment-intensive nature, may (with the Bank's prior agreement) be carried out by Municipalities through force account, in accordance with the provisions of said paragraph of the Guidelines, as prescribed in the Operational Manual.

Part D:

Review by the Bank of Procurement Decisions

1.

Procurement Planning

Prior to the issuance of any invitations 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 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

With respect to: (a) each contract for works to be procured in accordance with the procedures referred to in Part B above; (b) (i) each contract for works estimated to cost more than \$1,000,000 equivalent; and (ii) the first two contracts for works to be procured in accordance with the procedures referred to in Part C.1 above; and (c) each contract for works to be procured in accordance with the procedures referred to in Part C.3 above, the procedures set forth in paragraphs 2 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

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 Bank Borrowers" published by the Bank in January 1997 and revised in September 1997 and January 1999 (the Consultant Guidelines) and the following provisions of Sections II and III of this Schedule.

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, 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.

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Part C:

Other Procedures for the Selection of Consultants

1.

Selection Based on Consultants' Qualifications

Services estimated to cost \$100,000 equivalent per contract or less 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 of NGOs working with Communities and Community-based Micro-enterprises

under Part F of the Project 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 tasks that meet the requirements set forth in paragraph 5.1 of the Consultant Guidelines and not exceeding in the aggregate \$3,600,000 equivalent, 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.

2.

Prior Review

(a)

With respect to: (i) each contract for the employment of consulting firms estimated to cost \$100,000 equivalent or more; and (ii) each contract for the employment of NGOs to be awarded under Part C.2 hereof, 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 less than \$100,000 equivalent, the terms of reference and short list of the consulting firms shall be furnished to the Bank for its prior review and approval. The contract shall be awarded only after the said approval shall have been given.

(c)

With respect to each contract for the employment of individual consultants estimated to cost \$50,000 equivalent 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 the said approval shall have been given.

(d)

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

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 Consultant Guidelines shall apply.

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Section III.

Special Provisions

A.

In addition and without limitation or restriction to any other provision set forth in this Schedule or the Guidelines, the following provisions shall govern all procurement of works under Part C.1 of Section I of this Schedule:

1.

No reference value shall be required for publication in the bidding documents.

2.

Award of contracts shall be based exclusively on price and, whenever appropriate, shall take into account factors that can be quantified objectively, and the procedure for such quantification shall be disclosed in the invitation to bid.

3.

The Borrower shall utilize standard bidding documents satisfactory to the Bank.

B.

In addition and without limitation or restriction to any other provision set forth in this Schedule or the Consultant Guidelines, the following provisions shall govern all employment of consultants referred to in Section II of this Schedule:

1.

Foreign consultants shall not be required to be locally registered as a condition of participation in the selection process.

2.

No reference value shall be required for publication in the proposal documents.

3.

No minimum number of responsive proposals shall be required prior to awarding a contract for consulting services.

4.

Foreign consultants shall not be required to legalize their proposals or any documentation related to such proposals with either Peruvian consulates, the Ministry of Foreign Affairs, or any Peruvian authorities, as a pre-condition to participating in the selection process.