

CONFORMED COPY

LOAN NUMBER 4735-BR

Loan Agreement

(Maranhão Integrated Program: Rural Poverty Reduction Project)

between

**INTERNATIONAL BANK FOR RECONSTRUCTION
AND DEVELOPMENT**

and

STATE OF MARANHÃO

Dated February 15, 2006

LOAN NUMBER 4735-BR

LOAN AGREEMENT

AGREEMENT, dated February 15, 2006, between the INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT (the Bank) and the STATE OF MARANHÃO (the Borrower).

WHEREAS (A) the Federative Republic of Brazil (the Guarantor) and the Borrower, having been satisfied as to the feasibility and priority of the project described in Schedule 2 to this Agreement (the Project), have requested the Bank to assist in the financing of the Project;

(B) by an agreement of even date herewith between the Guarantor and the Bank (the Guarantee Agreement), the Guarantor has agreed to guarantee the payment obligations of the Borrower in respect of the loan provided for in Article II of this Agreement (the Loan); and

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:

(a) "Approved POA" means each approved annual operating plan referred to in Section 3.04 (b) of this Agreement;

(b) "Area A Grants" means grants to be made by the Borrower to finance Community Subprojects in the 80 Municipalities with the lowest HDI-M;

(c) "Area B Grants" means grants to be made by the Borrower to finance Community Subprojects in Municipalities other than the Municipalities referred to in (b) above;

(d) "COFIEEX" means *Comissão de Financiamentos Externos*, the Guarantor's Commission of External Borrowings, within the Guarantor's Ministry of Planning, Budget and Management, and governed by the Guarantor's Decree (*Decreto*) No. 3502, of June 12, 2000;

(e) "Community Association" means a civil association formed by members of a community (*associação civil*) duly established in the Borrower's territory in accordance with the Guarantor's laws, and which meets the criteria set forth in the Operational Manual for participating in the Project;

(f) "Community Subproject" means any investment referred to in Part A of the Project to be carried out by a Community Association utilizing the proceeds of a Grant, and which meets the criteria set forth in the Operational Manual;

(g) "Eligible Categories" means categories (1) through (4) set forth in the table in Part A.1 of Schedule 1 to this Agreement;

(h) "Eligible Expenditures" means the expenditures for goods, works and services referred to in Section 2.02 of this Agreement;

(i) "FMR" means each financial monitoring report prepared in accordance with Section 4.02 of this Agreement;

(j) "GEPLAN" means *Gerência de Estado de Planejamento, Orçamento e Gestão*, the Borrower's unit responsible for planning, budget and management;

(k) "Grant" means an Area A Grant or an Area B Grant;

(l) "Grant Agreement" means any of the agreements to be entered into between the Borrower and a Community Association providing for a Grant;

(m) "HDI" means the Borrower's human development index, which is measured by the Guarantor's *Instituto de Pesquisas Econômicas Aplicadas - IPEA* on the basis of the indicators for health, education and income in the Borrower's territory;

(n) "HDI-M" means the human development index of a Municipality, which is measured by *Fundação João Pinheiro* on the basis of the indicators for health, education and income in such Municipality's territory;

(o) "MIS" means the Project monitoring and information system referred to in Section 3.03 (a) of this Agreement;

(p) "Municipal Council" means a municipal council, composed mainly of representatives of communities and local organizations in a Municipality, as provided in the Operational Manual;

(q) "Municipality" means any municipality in the Borrower's territory, except the Municipality of São Luís;

(r) "Operational Manual" means the manual referred to in Section 3.01 (b) (iii) of this Agreement, as the same may be amended from time to time with the agreement of the Bank;

(s) "Report-based Disbursements" means disbursements made pursuant to the Borrower's option for withdrawal of funds from the Loan Account referred to in Part A.5 of Schedule 1 to this Agreement;

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

(u) "STU" means State Technical Unit (*Núcleo Estadual de Projetos Especiais*) within the Borrower's management unit of agriculture and rural development (*Gerência de Estado de Agricultura, Pecuária e Desenvolvimento Rural - GEAGRO*), and which is the Project coordination and technical unit established pursuant to the Borrower's Decree No. 15,605, of June 11, 1997.

ARTICLE II

The Loan

Section 2.01. The Bank agrees to lend to the Borrower, on the terms and conditions set forth or referred to in this Agreement, the amount of thirty million Dollars (\$30,000,000).

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 goods, works and services required for the Project and to be financed out of the proceeds of the Loan, as well as in respect of the fee referred to in Section 2.04 of this Agreement.

Section 2.03. The Closing Date shall be December 31, 2008 or such later date as the Bank shall establish, after having received evidence that COFIEX has authorized the extension of the Closing Date. The Bank shall promptly notify the Borrower and the Guarantor of such later date, which shall not be a date beyond the date authorized by COFIEX.

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 and the Guarantor 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 2.06, 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 and the Guarantor of the new basis. The new basis shall become effective on the expiry of the notice period unless the Borrower or the Guarantor notifies the Bank during said period of its objection thereto, in which case said modification shall not apply to the Loan.

Section 2.07. Interest and other charges shall be payable semiannually in arrears on May 15 and November 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. (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, shall carry out: (i) Parts A, B and D of the Project through STU with the assistance of the Municipal Councils and the Municipalities; and (ii) Part C of the Project through GEPLAN, all with due diligence and efficiency and in conformity with appropriate social, administrative, agricultural, environmental, financial and engineering practices, and shall provide or cause to be provided, promptly as needed, the funds, facilities, services and other resources required for the Project.

(b) Without limitation to the provisions of Section 3.01 (a) of this Agreement, the Borrower shall, as applicable, carry out, and cause to be carried out, the Project in accordance with the provisions and/or recommendations of:

- (i) the Approved POA;
- (ii) the plan, furnished by the Borrower to the Bank on October 30, 2003, for the development of indigenous peoples carrying out Community Subprojects, or benefiting in any manner from the carrying out of the Project, with the assistance of the Guarantor's *Fundação Nacional do Índio* (FUNAI); and
- (iii) a manual, satisfactory to the Bank (the Operational Manual), which shall contain the policies and procedures for the carrying out, monitoring and evaluation of the Project, including, inter alia: (A) the procedures for preparation, prioritization and approval of Community Subprojects, including environmental criteria and procedures for screening and management of such Subprojects, as provided in the environmental management plan furnished by the Borrower to the Bank on October 30, 2003, and the expected contribution of such Subprojects to a positive impact on the HDI; (B) the criteria for eligibility of Community Associations to participate in the Project, (C) the organization and membership of Municipal Councils; (D) the responsibilities and functions of the Municipal Councils in the selection of Community Associations and Community Subprojects; (E) the procedures and criteria for the provision of Area A Grants and Area B Grants; (F) the model form of Grant Agreements; (G) the Project procurement and financial management requirements and

procedures; and (H) the indicators to be used for Project monitoring and evaluation. In case of any inconsistency between a provision of the Operational Manual and this Agreement, the provision of this Agreement will prevail.

(c) The Borrower shall maintain the STU, during Project implementation, with responsibilities, structure and functions satisfactory to the Bank.

Section 3.02. 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 this Agreement.

Section 3.03. The Borrower shall:

(a) establish and maintain a Project monitoring and information system, satisfactory to the Bank (the MIS), to enable it to monitor and evaluate on an on-going basis, in accordance with the performance indicators set forth in the Operational Manual, the carrying out of the Project and the achievement of the objective thereof;

(b) prepare, under terms of reference satisfactory to the Bank, and furnish to the Bank, not later than six months after the Effective Date, the baseline evaluation study referred to in Part D.4 of the Project;

(c) prepare, under terms of reference satisfactory to the Bank, and furnish to the Bank, not later than twelve months after the Effective Date and yearly thereafter during 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 period preceding the date of such report and setting out the measures recommended to ensure the efficient carrying out of the Project and the achievement of the objective thereof during the period following such date; and

(d) review such report with the Bank promptly after its preparation, and, thereafter, take all measures required to ensure the efficient completion of the Project and the achievement of the objective thereof, based on the conclusions and recommendations of the said report and the Bank's views on the matter.

Section 3.04. The Borrower shall:

(a) by October 30 of each year during Project implementation, prepare and furnish to the Bank the proposed annual operating plans and budget, satisfactory to the

Bank, detailing the Project activities proposed to be carried out during the next succeeding year and the respective sources of funding therefor; and

(b) not later than 30 days after the approval of the Borrower's budget by its *Assembléia Legislativa* (Legislative Assembly), furnish to the Bank the approved annual operating plans and respective budget (Approved POA) referred to in paragraph (a) of this Section for each year in question.

Section 3.05. The Borrower shall:

(a) furnish to the Bank, not later than twelve months after the Effective Date and yearly thereafter during the period of Project implementation, the results and recommendations of an assessment, to be carried out under terms of reference satisfactory to the Bank, on the cost structure and effectiveness of Community Subprojects, including an evaluation of the physical performance, and cost comparisons and procurement procedures thereof;

(b) review with the Bank the results and recommendations of such assessments; and

(c) take or cause to be taken all such action which shall have been agreed by the Bank and the Borrower during the review referred to in paragraph (b) above, as shall be necessary for the efficient implementation of Community Subprojects, such action to be taken in a manner and within a timetable agreed upon during such review.

Section 3.06. In carrying out Part C of the Project, the Borrower shall:

(a) not later than March 31 of each year during the carrying out of such Part C, review with the Bank the Borrower's proposed program of public expenditures related to the Project for the next succeeding year and its impact on poverty reduction in the Borrower's territory; and

(b) take into account, in the carrying out of such program, the Bank's views thereon.

Section 3.07. For the purposes of Section 9.07 (c) of the General Conditions, the Borrower 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 future operation of the Project; 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 shall establish and maintain, as part of the MIS, a financial management system, including records and accounts, and prepare financial statements in accordance with consistently applied accounting standards acceptable to the Bank, adequate to reflect the operations, resources and expenditures related to the Project.

(b) The Borrower shall:

- (i) have the financial statements referred to in paragraph (a) of this Section for each fiscal year (or other period agreed to by the Bank) audited, in accordance with consistently applied auditing standards acceptable to the Bank, by independent auditors acceptable to the Bank;
- (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 (or such other period agreed to by the Bank): (A) certified copies of the financial statements referred to in paragraph (a) of this Section for such year (or such other period agreed to by the Bank), as so audited; and (B) an opinion on such statements by said auditors, in scope and detail satisfactory to the Bank; and
- (iii) furnish to the Bank such other information concerning such records and accounts, and the audit of such financial statements, 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 Report-based Disbursements or were made on the basis of statements of expenditure, the Borrower shall:

- (i) retain, until at least one year after the Bank has received the audit report for, or covering, 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;
- (ii) enable the Bank's representatives to examine such records; and
- (iii) ensure that the relevant statements of expenditure and reports referred to in Part A.5 of Schedule 1 to this Agreement, as the case may be, are included in the audit for each fiscal year (or other period agreed to by the Bank), referred to in paragraph (b) of this Section.

Section 4.02. (a) Without limitation upon the Borrower's reporting obligations set out in Section 3.03 of this Agreement, the Borrower shall prepare and furnish to the Bank a financial monitoring report, in form and substance satisfactory to the Bank (the FMR), which:

- (i) sets forth sources and uses of funds for the Project, both cumulatively and for the period covered by said report, showing separately funds provided by the Loan, and explains variances between the actual and planned uses of such funds;
- (ii) describes physical progress in Project implementation, both cumulatively and for the period covered by said report, and explains variances between the actual and planned Project implementation;
- (iii) sets forth the status of procurement under the Project, as at the end of the period covered by said report; and
- (iv) presents projections, for a period until the end of the fiscal year following the date of the FMR, of physical progress, procurement activities, and sources and uses of funds in respect of the Project.

(b) The first FMR shall be furnished to the Bank not later than 45 days after the end of the first calendar quarter after the Effective Date, and shall cover the period from the incurrence of the first expenditure under the Project through the end of such first calendar quarter; thereafter, each FMR shall be furnished to the Bank not later than 45

days after each subsequent calendar quarter, and shall cover the period not covered by the previous FMR until the end of such calendar quarter.

ARTICLE V

Effective Date; Termination

Section 5.01. 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) the Borrower has adopted the Operational Manual; and

(b) the Borrower has furnished to the Bank the terms of reference for the baseline evaluation study, and the overall Project evaluation framework, as required for the impact evaluation to be carried out under Part D.4 of the Project.

Section 5.02. The following is specified as an additional matter, within the meaning of Section 12.02 (c) of the General Conditions, to be included in the opinion or opinions to be furnished to the Bank, namely that the Loan has been duly registered by the Guarantor's Central Bank.

Section 5.03. The date May 16, 2006 is hereby specified for the purposes of Section 12.04 of the General Conditions.

ARTICLE VI

Representative of the Borrower; Addresses

Section 6.01. The Manager of GEPLAN is designated as representative of the Borrower for the purposes of Section 11.03 of the General Conditions.

Section 6.02. The following addresses are specified for the purposes of Section 11.01 of the General Conditions:

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 Washington, D.C.	248423 (MCI) or 64145 (MCI)	(202) 477-6391

For the Borrower:

Gerência de Estado de Planejamento, Orçamento e Gestão - GEPLAN
Avenida Jerônimo de Albuquerque s/n
65051-200 São Luís, Maranhão
Brazil

Facsimile: (55-98) 227-5645

With copy to:

SEAIN - Secretaria de Assuntos Internacionais do
Ministério do Planejamento, Orçamento e Gestão
Esplanada dos Ministérios - Bloco K - 5º andar
70040-906 Brasília, DF
Brazil

Facsimile: (55-61) 225-4022

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, Brazil, as of the day and year first above written.

INTERNATIONAL BANK FOR
RECONSTRUCTION AND DEVELOPMENT

By /s/ John Briscoe

Authorized Representative

STATE OF MARANHÃO

By /s/ José Reinaldo Carneiro Tavares

Authorized Representative

SCHEDULE 1

Withdrawal of the Proceeds of the Loan

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:

<u>Category</u>	<u>Amount of the Loan Allocated (Expressed in Dollars)</u>	<u>% of Expenditures to be Financed</u>
(1) Grants:		75% of the expenditures for goods, works and services for a Community Subproject
(a) Area A Grants	16,000,000	
(b) Area B Grants	10,600,000	
(2) Consultants' services under Parts B, C and D of the Project	800,000	84%
(3) Training under Parts B, C and D of the Project	600,000	100%
(4) Administrative Costs:		
(a) incremental operational costs	100,000	20%
(b) Project supervision and monitoring costs	300,000	50%

<u>Category</u>	<u>Amount of the Loan Allocated (Expressed in Dollars)</u>	<u>% of Expenditures to be Financed</u>
(5) Fee	300,000	Amount due under Section 2.04 of this Agreement
(6) Unallocated	<u>1,300,000</u>	
TOTAL	<u>30,000,000</u>	

2. For the purposes of this Schedule the term "Administrative Costs" means the operational costs (which would not have been incurred absent the Project) and the supervision and monitoring costs of the Project incurred by the STU under Part D of the Project (excluding expenditures for salaries and related benefits and for training).

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 exceeding \$3,000,000, may be made on account of payments made within twelve months prior to the date of this Agreement, but in no case prior to June 30, 2003;

(b) payments under a Grant unless the respective Grant Agreement shall have been entered into between the parties thereto; and

(c) payments under a Grant for a Community Subproject costing more than the equivalent of \$50,000, unless the Bank shall have approved such Community Subproject.

4. The Bank may require withdrawals from the Loan Account to be made on the basis of statements of expenditure for expenditures, all under such terms and conditions as the Bank shall specify by notice to the Borrower:

(a) under contracts for goods or works costing less than the equivalent of \$100,000 per contract;

(b) for services of individual consultants and consulting firms under contracts not exceeding \$50,000 and \$100,000 equivalent per contract, respectively; and

(c) for training and administrative costs.

5. The Borrower may request withdrawals from the Loan Account to be made on the basis of reports to be submitted to the Bank in form and substance satisfactory to the Bank, such reports to include the FMR and any other information as the Bank shall specify by notice to the Borrower (Report-based Disbursements). In the case of the first such request submitted to the Bank before any withdrawal has been made from the Loan Account, the Borrower shall submit to the Bank only a statement with the projected sources and applications of funds for the Project for the six-month period following the date of such request.

B. Special Account

1. The Borrower may 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) if the Borrower is not making Report-based Disbursements, withdrawals shall be made in accordance with the provisions of Annex A to this Schedule 1; and

(b) if the Borrower is making Report-based Disbursements, 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 at any time is not satisfied that the reports referred to in Part A.5 of this Schedule 1 adequately provide the information required for Report-based Disbursements;

(b) if the Bank determines at any time that all further withdrawals for payment of Eligible Expenditures 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 Report-based Disbursements or were made on the basis of statements of expenditure, as the case may be.

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 and the Guarantor 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 and the Guarantor 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. Unless the Bank shall otherwise agree, no further deposit by the Bank into the Special 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 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 subparagraph (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
Report-based Disbursements**

1. For the purposes of this Annex, the term “Authorized Allocation” means the amount of \$3,000,000 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 the amount of \$2,000,000 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 be equal to or exceed \$8,000,000.

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 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
Report-based Disbursements**

1. 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. 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 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 reports referred to in Part A.5 of this Schedule 1 applicable to such withdrawal application, is required to be deposited in order to finance Eligible Expenditures during the six-month period following the date of such reports.

SCHEDULE 2

Description of the Project

The objective of the Project is to foster an increase in the Borrower's HDI, directly through a community-driven development approach, and indirectly by supporting the Borrower's efforts to integrate, monitor and evaluate its overall investment program and policies cross-sectorally for greater effectiveness in poverty reduction.

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: Community Subprojects

Financing of demand driven projects (the Community Subprojects) in about 216 Municipalities consisting, *inter alia*, of: (a) socio-economic infrastructure investments, such as community school construction, establishment of rural health posts, rural access road improvement, establishment of community day-care and community centers, installation of sanitation facilities, acquisition and utilization of distance learning equipment, establishment of training centers, installation of water systems and rural electrification; (b) production investments, such as small-scale agro-industry, handicrafts, irrigation schemes and tourism promotion; and (c) environmental investment, such as recycling, watershed protection, community forestry, non-timber forest products, and forest fire prevention equipment for community use.

Part B: Institutional Development

1. Provision of technical assistance and training for Community Associations in, *inter alia*, organization and strengthening of such Associations, identification, preparation, and operation of Community Subprojects, and maintenance of the investments under such Subprojects.
2. Carrying out of capacity-building programs for Municipal Councils and Community Associations, including provision of training on the role of Municipal Councils, the contents of the Operational Manual, evaluation and supervision of Community Subprojects, environmental assessment of such Subprojects, and participatory planning and financial management related to such Subprojects, and provision of computers to Municipal Councils to assist them in performing their functions under Community Subprojects.

3. Provision of on-the-job training and expert advice for the STU, Municipal Councils, and Community Associations on technical matters regarding preparation, execution and operation of Community Subprojects, including development of standard project designs, monitoring techniques and financial management.
4. Provision of technical assistance (through consultants' services, studies and training) to GEPLAN for the implementation of the administrative and other reforms required for the modernization of the Borrower's administrative and fiscal structure in the context of increasing the Borrower's HDI.
5. Carrying out of workshops and seminars for Municipal Councils and Community Associations to exchange views and disseminate information and experience with respect to the carrying out of the Project among themselves and with other states in the northeast region of Brazil.

Part C: State Governance and Capacity Building

Provision of technical assistance (including training to the relevant staff) for the integration of the Borrower's and Guarantor's policies for poverty reduction in order to avoid duplication of actions, and the strengthening of the Borrower's management capacity to better monitor the impact of its public expenditures to reduce poverty in rural areas.

Part D: Project Administration

Support to the overall Project implementation, coordination and supervision including, *inter alia*:

1. the operation of the STU and its field offices related to Project implementation, including provision of training to the relevant staff;
2. the establishment and operation of the MIS, including provision of training to the relevant staff;
3. the design, development and carrying out of a campaign within the Borrower's territory to disseminate information about the Project; and
4. the carrying out of studies to assess the impact of the Project, including, *inter alia*, a baseline evaluation study, annual physical performance reviews, a mid-term implementation review, and a comprehensive impact evaluation.

* * *

The Project is expected to be completed by June 30, 2008.

SCHEDULE 3

Amortization Schedule

<u>Date Payment Due</u>	<u>Payment of Principal (Expressed in Dollars) *</u>
On each May 15 and November 15	
beginning November 15, 2009 through May 15, 2021	1,250,000

* 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 Goods and Works

Part A: General

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 Bank 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.

Part B: Procurement Procedures

1. National Competitive Bidding

Except as provided in paragraphs 2, 3 and 4 below, goods and works shall be procured under contracts awarded in accordance with the provisions of paragraphs 3.3 and 3.4 of the Guidelines, using standard bidding documents acceptable to the Bank. Without limitation to any other provisions set forth in this Schedule or the Guidelines, the following shall apply to the procurement of goods and/or works to be undertaken pursuant to this Part B.1:

(a) Contracts shall be awarded to the bidder whose bid has been determined to be the lowest evaluated bid, such evaluation to be based on price and, whenever appropriate, to also take into account factors similar to those referred to in paragraph 2.51 of the Guidelines, provided, however, that the bid evaluation shall always be based on factors that can be quantified objectively, and the procedure for such quantification shall be disclosed in the invitation to bid.

(b) Whenever required by the Bank, the invitation to bid shall be advertised for at least three consecutive days in a newspaper of wide circulation in Brazil.

(c) The arrangements, under the invitation to bid, for a joint-venture (*consórcio*) of Brazilian and foreign firms shall be approved in advance by the Bank in each case.

(d) The invitation to bid shall not establish, for purposes of acceptance of bids, minimum or maximum amounts for the contract prices.

(e) The purchaser shall not, without the Bank's prior approval, issue any change order under a contract which would increase or decrease by more than 15% the quantity of goods (and related services) without any change in the unit prices or other terms and conditions of sale.

2. National Shopping

Except as provided in paragraph 4 below, goods estimated to cost less than \$100,000 equivalent per contract, up to an aggregate amount of \$1,500,000 equivalent, may be procured under contracts awarded on the basis of national shopping procedures in accordance with the provisions of paragraphs 3.5 and 3.6 of the Guidelines, including, as a form of such shopping, the bidding (*pregão*) procurement system set forth in the Guarantor's Law No. 10,520 of July 17, 2002.

3. Procurement of Small Works

Except as provided in paragraph 4 below, works estimated to cost less than \$100,000 equivalent per contract, up to an aggregate amount of \$1,000,000 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.

4. Community Participation

Goods and works costing \$50,000 equivalent or less per contract under Community Subprojects to be carried out in scattered or remote areas, may be procured in accordance with procedures for community participation, acceptable to the Bank, as provided in paragraph 3.15 of the Guidelines (including direct contracting in accordance with the provisions of paragraph 3.7 of the Guidelines), all as set forth in the Operational Manual.

Part C: 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. Such plan shall be updated every twelve months during the execution of the Project, and each such updating shall be furnished to the Bank for its review and approval. Procurement of all goods and works shall be undertaken in accordance with such procurement plan (as updated) 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 to be procured pursuant to the provisions of Part B.1 of this Section, the procedures set forth in paragraphs 2 and 3 of Appendix 1 to the Guidelines shall apply.

(b) With respect to the first contract for goods and the first contract for works to be procured in accordance with the procedures referred to in Parts B.2 and B.3 of this Section, the following procedures shall apply:

- (i) prior to the selection of any supplier or contractor, the Borrower shall provide to the Bank a report on the comparison and evaluation of quotations received;
- (ii) prior to the execution of any contract, the Borrower shall provide to the Bank a copy of the specifications and the draft contract; and
- (iii) the procedures set forth in paragraph 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

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, January 1999 and May 2002 (the Consultant Guidelines), paragraph 1 of Appendix 1 thereto, Appendix 2 thereto, and the following provisions of this Section II.

Part B: Quality- and Cost-based Selection

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, and the provisions of paragraphs 3.13 through 3.18 thereof applicable to quality- and cost-based selection of consultants.

Part C: Other Procedures for the Selection of Consultants

1. Least-cost Selection

Services for routine assignments estimated to cost less than \$200,000 equivalent per contract may be procured under contracts awarded in accordance with the provisions of paragraphs 3.1 and 3.6 of the Consultant Guidelines.

2. Individual Consultants

Services of individual consultants for tasks that meet the requirements set forth in paragraph 5.1 of the Consultant Guidelines: (a) shall be procured under contracts awarded in accordance with the provisions of paragraphs 5.1 through 5.3 of the Consultant Guidelines; or (b) may be selected on a sole-source basis in accordance with the provisions of paragraphs 5.3 and 5.4 of the Consultant Guidelines, subject to prior approval of the Bank.

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

1. Selection Planning

A plan for the selection of consultants, which shall include contract cost estimates, contract packaging, and applicable selection criteria and procedures, shall be furnished to the Bank prior to the issuance to consultants of any requests for proposals. Such plan shall be updated every twelve months during the execution of the Project, and each such updating shall be furnished to the Bank for its review and approval. Selection of all consultants' services shall be undertaken in accordance with such selection plan (as updated) as shall have been approved by the Bank.

2. Prior Review

(a) The procedures set forth in paragraphs 2, 3 and 5 of Appendix 1 to the Consultant Guidelines shall apply to each contract for the employment of consulting firms estimated to cost the equivalent of \$100,000 or more.

(b) With respect to each contract for the employment of an individual consultant, estimated to cost the equivalent of \$50,000 or more, the report on the qualifications and experience of all evaluated candidates, and the terms of reference and terms of employment of the consultant 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. The provisions of paragraph 3 of Appendix 1 to the Consultant Guidelines shall also apply to such contract.

3. Post Review

The procedures set forth in paragraph 4 of Appendix 1 to the Consultant Guidelines shall apply to each contract not governed by paragraph 2 of this Part D.