

CONFORMED COPY

LOAN NUMBER 3101 ME

(Water, Women and Development Project)

between

INTERNATIONAL BANK FOR RECONSTRUCTION
AND DEVELOPMENT

and

BANCO NACIONAL DE OBRAS Y SERVICIOS
PUBLICOS, S.N.C.

Dated September 25, 1989

LOAN NUMBER 3101 ME

LOAN AGREEMENT

AGREEMENT, dated September 25, 1989, between INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT (the Bank) and BANCO NACIONAL DE OBRAS Y SERVICIOS PUBLICOS, S.N.C. (the Borrower).

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

(B) by an agreement (the Guarantee agreement) of even date herewith between the Guarantor and the Bank, the Guarantor has agreed to guarantee the obligations of the Borrower in respect of the Loan, and to undertake such other obligations as set forth in the Guarantee Agreement;

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" of the Bank, dated January 1, 1985, with the last sentence of Section 3.02 is deleted (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) "Special Account" means the account referred to in Section 2.02 (b) of this agreement;

(b) "General Interest Rate Agreement" means the General Agreement on Interest Rates Applicable to Credit Operations of Fondos de Fomento financed by the International Bank for Reconstruction and Development between the Guarantor and the Bank, dated August 7, 1984, as such agreement may be amended from time to time;

(c) "Eligible State" means each of the State of Queretaro, the State of Michoacan or the State of Hidalgo in the territory of the Guarantor; and "Eligible States" means the States of Queretaro, Michoacan and Hidalgo collectively;

(d) "SWA" means each of the following State Water Agency of an Eligible State having juridical personality and the capacity to contract under the laws of the Guarantor or the Eligible State, and to which the Borrower has made or proposes to make a Subsidiary Loan (as hereinafter defined): Comision Estatal de Aguas, created by Decree of the State of Queretaro, published in the Periodico Oficial of such State, dated March 13, 1980; Sistema de Agua Potable y Alcantarillado de Morelia, created by Decree No. 216 of the State of Michoacan, published in the Periodico Oficial of such State, dated February 25, 1985; and Comision de Servicios de Aguas del Estado de Hidalgo, created by Decree No. 38 of the State of Hidalgo, published in the Periodico Oficial of such State, dated April 1, 1977; and such entities to be collectively called "SWAs";

(e) "Subsidiary Loan" means a loan made or proposed to be made by the Borrower to a SWA, partially financed out of the proceeds of the Loan, to be utilized by the SWA in carrying out Part A of the Project, including the financing of a Sub-project (as hereinafter defined) in an Eligible State; and "Subsidiary Loan Agreement" means the agreement between the Borrower, the SWA and the relevant Eligible State providing for such Subsidiary Loan, as such agreement may be amended from time to time;

(f) "Sub-project" means a specific investment project, for the installation and maintenance of water supply and sanitation services, in an Eligible State included in Part A.1 of the Project;

(g) "Financial Intermediary" means each of the following credit institutions having juridical personality and the capacity to contract under the laws of the Guarantor or an Eligible State and qualified by the Borrower and the Bank to be eligible to participate in making Investment Subloans (as hereinafter defined) under Part B.1 of the Project and each of which shall have entered into a Participation Agreement (as hereinafter defined) with the Borrower: Fondo de Financiamiento y Garantia para el Desarrollo de La Micro y Pequena Industrias y de las Empresas del Sector Social

de la Economia de Queretaro (FIMINSSE) created by the Convenio Modificatorio al Contrato de Fideicomiso, published in the Periodico Oficial of the State of Queretaro, dated March 23, 1988; Fondo Mixto para el Fomento Industrial de Michoacan (FOMICH), created by Ley No. 70 of the State of Michoacan, published in the Periodico Oficial of such State, dated March 11, 1976; and La Compania Impulsora Hidalguense de Industria y Comercio, S.A. de C.V. (IHIC), created by Decree No. 70 of the State of Hidalgo, published in the Periodico Oficial of such State, dated March 11, 1976;

(h) "Investment Subloan" means a loan made, or proposed to be made, in accordance with the terms and conditions set forth in Schedule 8 to this Agreement, by a Financial Intermediary to a Project Beneficiary (as hereinafter defined) and to be partially financed out of the proceeds of the Loan for the purpose of partly financing an Investment (as hereinafter defined) in a relevant Eligible State under Part B.1 of the Project;

(i) "Project Beneficiary" means a person, group of persons, or an entity in the Eligible States having juridical personality and the capacity to contract under the laws of the Guarantor or an Eligible State, and to whom or which a Financial Intermediary has made, or proposes to make, an Investment Subloan;

(j) "Investment" means an investment in productive activities carried out, or to be carried out, by a Project Beneficiary in a relevant Eligible State utilizing the proceeds of an Investment Subloan including the establishment and operation of microenterprises, and investment in working capital required for such activities including tools and raw materials required to carry out piecemeal work for in-bond industries;

(k) "Participation Agreement" means the agreement to be entered into, pursuant to Section 3.03 (a) (ii) of this Agreement, between the Borrower and each Financial Intermediary and Eligible State for purposes of carrying out Part B of the Project, including making Investment Subloans to Project Beneficiaries;

(l) "IDEAS" means Instituto de Desarrollo Economico y de Asistencia Social, an agency of the State of Queretaro responsible for carrying out social action programs;

(m) "Promotion Agency" means each of FOMICH, IHIC and IDEAS; such entities are collectively referred to as "Promotion Agencies";

(n) "Pesos" means the currency of the Guarantor;

(o) "Annual Water Plan" means the plan of each SWA describing the proposed investments in water supply and sanitation services to be made during the following fiscal year;

(p) "SPS" means the State Planning Secretariat of each Eligible State;

(q) "Health Education Program" means a program to improve the health and sanitation habits of members of communities in the Eligible States and referred to in Section 3.02 of the Guarantee Agreement; and

(r) "SSA" means Secretariat of Health of the Guarantor.

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 the Loan Agreement, various currencies that shall have an aggregate value equivalent to the amount of twenty million dollars (\$20,000,000), being the sum of withdrawals of the proceeds of the Loan, with

each withdrawal valued by the Bank as of the date of such withdrawal.

Section 2.02. (a) The amount of the Loan may be withdrawn from the Loan Account in accordance with the provisions of Schedule 1 to this Agreement, as such Schedule may be amended from time to time by agreement between the Bank and the Borrower, for expenditures made, or, if the Bank shall so agree, to be made, in respect of the reasonable cost of goods and services required for the Project described in Schedule 2 to this agreement and to be financed out of the proceeds of the Loan.

(b) The Borrower shall, for the purposes of the Project, open and maintain in dollars a Special Account on terms and conditions satisfactory to the Bank. Deposits into, and payments out of, the Special Account shall be made in accordance with the provisions of Schedule 5 to this Agreement.

Section 2.03. The Closing Date shall be December 31, 1995, or such later date as the Bank shall establish. The Bank shall promptly notify the Borrower and the Guarantor of such later date.

Section 2.04. 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 2.05. (a) The Borrower shall pay interest on the principal amount of the Loan withdrawn and outstanding from time to time at a rate per annum for each Interest Period equal to half of one percent per annum above the Cost of Qualified Borrowings for the last Semester ending prior to the commencement of such Interest Period.

(b) As soon as practicable after the end of each Semester, the Bank shall notify the Guarantor and the Borrower of the Cost of Qualified Borrowings for such Semester.

(c) For purposes of this Section:

- (i) "Interest Period" means the six-month period commencing on each date specified in Section 2.06 of this Agreement, including the Interest Period in which this Agreement is signed;
- (ii) "Cost of Qualified Borrowings" means the cost of the outstanding borrowings of the Bank drawn down after June 30, 1982, expressed as a percentage per annum, as reasonably determined by the Bank; and
- (iii) "Semester" means the first six months or the second six months of a calendar year.

Section 2.06. Interest and other charges shall be payable semiannually on March 15 and September 15 in each year.

Section 2.07. 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; Transfer of Loan Proceeds

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 with the Participation of the SWAs, the Financial Intermediaries and the Eligible States, all with due diligence and efficiency and in conformity with appropriate technical, administrative, financial and environmental standards and practices, and shall provide, or

cause to be provided, in a timely manner as needed, the funds, facilities, services and other resources required for the Project.

Section 3.02. The Borrower shall enter into contractual arrangements, satisfactory to the Bank, with the Guarantor, providing, inter alia, for: (i) the transfer to the Guarantor of the proceeds of the Loan; (ii) the Guarantor's obligation to make available to the Borrower such portion of the proceeds of the Loan as shall be required by the Borrower to carry out Part C of the Project; (iii) the Guarantor's obligation to make available to the Borrower such portions of the proceeds of the Loan as shall be required by the Borrower to on-lend to the SWAs for purposes of carrying out Part A of the Project; (iv) the Guarantor's obligation to make available to the Borrower such portions of the proceeds of the Loan as shall be required by the Borrower to on-lend to the Financial Intermediaries for purposes of carrying out Part B of the Project; and (v) the transfer by the Guarantor to the Borrower of such funds as the Borrower shall be required to pay to the Bank on account of principal, interest and other charges on the Loan. Except as the Bank shall otherwise agree, the Borrower shall not change or fail to enforce any provision of such contractual arrangements.

Section 3.03. (a) Without any limitation or restriction upon any of its other obligations under the Loan Agreement, the Borrower shall: (i) make a Subsidiary Loan to each SWA for purposes of relending such portions of the proceeds of the Loan as shall be required by such SWA to carry out Part A of the Project in the relevant Eligible State, under a Subsidiary Loan Agreement, acceptable to the Bank, with each such SWA, all in accordance, inter alia, with the terms and conditions set forth or referred to in Schedule 6 to this Agreement; and (ii) enter into a Participation Agreement, acceptable to the Bank, with each Financial Intermediary, all in accordance, inter alia, with the terms and conditions set forth or referred to in Schedule 7 to this Agreement.

(b) Except as the Bank shall otherwise agree, the Borrower shall not change or fail to enforce any provision of such Subsidiary Loan Agreement or Participation Agreement.

(c) The Borrower shall inform the Bank of: (i) any proposed changes to such Subsidiary Loan Agreement or Participation Agreement in order to permit Bank review and approval of such proposed changes; and (ii) any breach or failure to enforce any provision of such Subsidiary Loan Agreement or Participation Agreement.

Section 3.04. The Borrower shall, in conjunction with each SWA, furnish to the Bank for its review and comment, no later than September 30 of each year until Project completion, the proposed Annual Water Plan of each SWA for the next following calendar year.

Section 3.05. The Borrower shall carry out supervision, monitoring and evaluation of the Project, with due diligence and efficiency and in conformity with appropriate technical, administrative and financial practices, and with management and staff adequate in numbers, qualifications and experience.

(b) Without restriction upon, or limitation to, the Borrower's other reporting requirements under this Agreement and the General Conditions, the Borrower shall provide semiannual reports, no later than March 31 and September 30 of each year, of such scope and in such detail and format as the Bank shall reasonably request, of the progress achieved toward implementing the Project.

Section 3.06. 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.

ARTICLE IV

Financial Covenants

Section 4.01. (a) The Borrower shall maintain, and shall cause each of the SWAs and the Financial Intermediaries to maintain, separate records and accounts adequate to reflect, in accordance with sound accounting practices, the operations, resources, and expenditures with respect to the execution of the Project, each Sub-project and each Investment.

(b) The Borrower shall cause:

- (i) the records, accounts and financial statements (balance sheets, statements of income and expenses and related statements) of the Borrower, each SWA and each Financial Intermediary and the records and accounts for the Special Account, for each fiscal year to be audited, in accordance with generally accepted auditing standards and procedures, consistently applied, by independent and qualified auditors;
- (ii) to be furnished to the Bank as soon as available, but in any case not later than six months after the end of each such year: (A) certified copies of its financial statements for such year as so audited, and (B) the report of such audit by said auditors, of such scope and in such detail as the Bank shall have reasonably requested;
- (iii) to be furnished to the Bank each month, certified statements of the Special Account; and
- (iv) to be furnished to the Bank such other information concerning said records, accounts and financial statements, as well as the audit thereof, as the Bank shall 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 statements of expenditure, the Borrower shall:

- (i) maintain or cause to be maintained, in accordance with paragraph (a) of this Section, separate records and accounts reflecting such expenditures;
- (ii) retain or cause to be retained, until at least one 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 separate records and accounts are included in the annual audit referred to in paragraph (b) of this Section and that the report thereof contains, in respect of such separate accounts, a separate opinion by said auditors as to whether the statement of expenditures 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.

ARTICLE V

Remedies of the Bank

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

(a) The Borrower or a SWA or the relevant Eligible State shall have changed, without the prior approval of the Bank, failed to enforce, or breached any provision of the relevant Subsidiary Loan Agreement.

(b) The Borrower or a Financial Intermediary or the relevant Eligible State shall have changed, without the prior approval of the Bank, failed to enforce, or breached any provision of the relevant Participation Agreement.

Section 5.02. Pursuant to Section 7.01 (h) of the General Conditions, the following additional event is specified: (a) that the event specified in paragraph (a) or (b) of Section 5.01 shall occur and shall continue for a period of sixty days after notice thereof shall have been given by the Bank to the Borrower, the Guarantor, and when appropriate, to the relevant SWA, Financial Intermediary or Eligible State.

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 and the Guarantor shall have entered into the contractual arrangements referred to in Section 3.02 of this agreement;

(b) that the Borrower shall have entered into a Subsidiary Loan Agreement referred to in Section 3.03 (a) (i) of this agreement with at least one SWA and the relevant Eligible State; and

(c) that the Borrower shall have entered into a Participation Agreement referred to in Section 3.03 (a) (ii) of the Agreement with at least one Financial Intermediary and the relevant Eligible State.

Section 6.02. The following are specified as additional matters, 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:

(a) that the contractual arrangements referred to in Section 3.02 of this Agreement have been duly authorized and are legally binding upon the parties thereto in accordance with their respective terms; and

(b) that the Subsidiary Loan Agreement and the Participation Agreement furnished to the Bank pursuant to paragraphs (b) and (c), respectively, of Section 6.01 of this agreement have been duly authorized and are legally binding upon the parties thereto in accordance with their terms.

Section 6.03. The date December 27, 1989, is hereby specified for the purposes of Section 12.04 of the General Conditions.

ARTICLE VII

Representative of the Borrower; Addresses

Section 7.01. The Director General 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 Bank:

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

Cable address:

INTBAFRAD
Washington, D.C.

Telex:

440098 (ITT)
248423 (RCA) or
64145 (WUI)

For the Borrower:

Banco Nacional de Obras y
Servicios Publicos, S.N.C.
Insurgentes Norte 423
06900 Mexico, D.F.
Mexico

Cable address:

BANTECARIO
Mexico, D.F. , Mexico

Telex:

BNDSME
01772619
Mexico City

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

INTERNATIONAL BANK FOR
RECONSTRUCTION AND DEVELOPMENT

By /s/ S. Shahid Husain
Regional Vice President
Latin America and the Caribbean

BANCO NACIONAL DE OBRAS Y
SERVICIOS PUBLICOS, S.N.C.

By /s/ Fernando del Villar Moreno
Authorized Representative

SCHEDULE 1

Withdrawal of the Proceeds of the Loan

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:

Category	Amount of the Loan Allocated (Expressed in Dollar Equivalent)	% of Expenditures to be Financed
(1) Civil Works for Sub-projects under Part A.1	9,000,000	50%

of the Project
and for priority
works under
Part C of the
Project

- | | | | |
|-----|--|-----------|--|
| (2) | Investment Subloans made by Financial Intermediaries under Part B.1 of the Project | 4,500,000 | 95% of amounts disbursed by Financial Intermediaries for Investment Subloans |
| (3) | Equipment and Materials under Parts A.2 and C | 2,000,000 | 100% of foreign expenditures and 40% of local expenditures |

Category	Amount of the Loan Allocated (Expressed in Dollar Equivalent)	% of Expenditures to be Financed
(4)	Technical assistance, training and consultant's services under Parts A.3, B.2 and C of the Project	2,500,000 100%
(5)	Unallocated	2,000,000
TOTAL	20,000,000	

2. For purposes of this Schedule:

(a) the term "foreign expenditures" means expenditures in the currency of any country other than that of the Guarantor, for goods or services supplied from the territory of any country other than that of the Guarantor; and

(b) the term "local expenditures" means expenditures in the currency of the Guarantor or for goods or services supplied from the territory of the Guarantor.

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 a total aggregate amount not exceeding the equivalent of \$1,500,000, may be made in respect of Categories (1) through (4) on account of payments made for expenditures before that date but after January 15, 1989, and, provided, however that such withdrawals are made within ninety days of the Effective Date of the Loan and in the case of the applicable Subsidiary Loan Agreements or the Participation Agreements referred to in clause (c) of this paragraph within ninety days of receiving the evidence referred to in such clause;

(b) disbursements made by the Borrower under Subsidiary Loans or by Financial Intermediaries under Investment Sub-loans, unless the Bank shall have received the evidence referred to in Section 2.02 of the General Interest Rate Agreement for said time period with respect to category I (1) or IV (i), respectively, of the table set forth in Schedule 1 to said Agreement, as amended, except as the Bank shall otherwise agree;

(c) payments made for expenditures under Subsidiary Loans and Investment Subloans for Parts A and B of the Project, respectively, unless the Bank shall have received satisfactory evidence that the applicable Subsidiary Loan Agreement and the

Participation Agreement which have not been furnished to the Bank pursuant to the provisions of paragraphs (b) and (c) of Section 6.01 of this Agreement shall have been entered into and furnished to the Bank, including a satisfactory legal opinion of counsel, acceptable to the Bank, that such Subsidiary Loan Agreement and Participation Agreement have been duly authorized by the Borrower and the respective Eligible States and are legally binding upon the parties thereto in accordance with their terms;

(d) payments made for expenditures under Part A of the Project by a SWA, unless the Bank shall have received a signed consultants' contract, satisfactory to the Bank, for its technical assistance program under Part A.3 of the Project; and

(e) payments made for expenditures under Part B of the Project by a Financial Intermediary, unless the Bank shall have received a signed consultant's contract, satisfactory to the Bank, for the program of technical assistance to the Promotion Agencies under Part B.2 of the Project.

SCHEDULE 2

Description of the Project

The objective of the Project is to improve the living standard of low-income population in selected States of Mexico by: (a) assisting the SWAs in the states of Michoacan, Queretaro and Hidalgo to establish an appropriate system for financing and implementing water and sanitation projects in low-income areas and strengthening their ability to design, build, operate and maintain these systems; (b) improving the target population's health and sanitation knowledge and habits; and (c) promoting income generating activities primarily among women who were hitherto engaged in fetching water and providing them with the necessary credit and training to carry out such activities.

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

Part A: Water and Sanitation Services

(1) Carrying out Sub-projects in selected low-income communities in rural and peri-urban areas in the Eligible States, such Sub-projects and communities to be selected in accordance with the methodology and by the entities specified in the Annex to this Schedule.

(2) Acquisition and utilization of equipment for the operation and maintenance of water systems.

(3) Technical assistance and training to strengthen the SWAs in the areas of organizational and operational performance, information systems, design and construction using low-cost technologies and in community mobilization techniques.

Part B: Income Generating Activities

(1) Financing of Investments in the Eligible States through the provision of Investment Subloans.

(2) Technical assistance to the Promotion Agencies consisting of: (a) training of the staff of the Promotion Agencies in participatory education techniques targeted mainly to women and in promotion and evaluation of Investments; (b) developing the decision-making and entrepreneurial skills of Project Beneficiaries; and (c) training of Project Beneficiaries in the skills required to carry out productive activities.

Part C: Project Preparation in Other States

Technical assistance to BANOBRAS for identifying and

preparing water-cum-productive activities projects in other States of the Guarantor including financing of priority works for such activities.

* * *

The Project is expected to be completed by June 30, 1995.

ANNEX TO SCHEDULE 2

Section I: Eligibility of Sub-projects

To be eligible for financing, a Sub-project must satisfy the following conditions:

(a) the works and designs proposed to be carried out under a Sub-project shall constitute the least cost solution; and

(b) Sub-projects shall have a per capita construction cost of not more than the equivalent of \$150 each.

Section II: Methodology for Selection of Communities

The communities in the Eligible States in which Sub-projects are carried out shall be selected in accordance with the following two-step procedure.

First Step: Screening of Communities

Potential communities shall be screened through a review of secondary data on the following:

(a) the estimated cost of bringing water to the community based on the characteristics of the water source;

(b) the degree of community marginality assessed on the basis of community access to schools, health centers, social and/or recreational facilities, churches, etc.; and

(c) the participatory experience of the community regarding its efforts towards individual and/or communal improvements.

Second Step: Application of Selection Criteria

After screening, communities shall be selected on the basis of the following criteria:

(a) the estimated cost of the Sub-projects;

(b) community commitment to the Sub-projects; and

(c) the potential for the successful implementation of productive activities in the community.

2. This methodology has been applied in selecting certain communities to be benefitted during the first year of Project implementation. The selection of the communities to be benefitted in subsequent years shall be carried out by the SPS of each Eligible State following the methodology outlined above in close collaboration with the respective SWA and the Promotion Agency.

SCHEDULE 3

Amortization Schedule

Date Payment Due	Payment of Principal (expressed in dollars)*
On each March 15 and September 15	
beginning March 15, 1995	
through March 15, 2006	835,000

On September 15, 2006

795,000

* The figures in this column represent dollar equivalents determined as of the respective dates of withdrawal. See General Conditions, Sections 3.04 and 4.03.

Premiums on Prepayment

Pursuant to Section 3.04 (b) of the General Conditions, the premium payable on the principal amount of any maturity of the Loan to be prepaid shall be the percentage specified for the applicable time of prepayment below:

Time of Prepayment	Premium
	The interest rate (expressed as a percentage per annum) applicable to the Loan on the day of prepayment multiplied by:
Not more than three years before maturity	0.18
More than three years but not more than six years before maturity	0.35
More than six years but not more than eleven years before maturity	0.65
More than eleven years but not more than fifteen years before maturity	0.88
More than fifteen years before maturity	1.00

SCHEDULE 4

Procurement of Goods and Works
and Consultants' Services

Section I. Procurement of Goods and Works

Part A: International Competitive Bidding

1. Except as provided in Part B hereof goods shall be procured under contracts awarded on the basis of international competitive bidding in accordance with procedures consistent with those set forth in Sections I and II of the "Guidelines for Procurement under IBRD Loans and IDA Credits" published by the Bank in May 1985 (the Guidelines).

2. To the extent practicable, contracts for goods shall be grouped in bid packages estimated to cost the equivalent of \$300,000 or more each.

Part B: Other Procurement Procedures

1. Local Competitive Bidding

Goods under contracts estimated to cost the equivalent of more than \$25,000 but less than the equivalent of \$300,000 per contract and all civil works estimated to cost the equivalent of more than \$25,000 per contract may be procured on the basis of

competitive bidding, advertised locally, in accordance with bidding procedures satisfactory to the Bank.

2. Local Shopping

Civil works and goods under contracts estimated to cost the equivalent of \$25,000 or less per contract may be procured on the basis of comparison of price quotations solicited from a list of at least three suppliers eligible under the Guidelines and in accordance with procedures acceptable to the Bank, provided, however, that the cost of civil works and goods procured under this paragraph shall not in the aggregate exceed the equivalent of US\$8,000,000.

3. Force Account

Civil works may be carried out by the SWAs, under force account, provided, however, that the cost of civil works carried out pursuant to this paragraph shall not exceed in the aggregate the equivalent of \$3,000,000.

4. Goods, Works and Services Financed under Investment Sub-loans

Goods, works and services financed out of the proceeds of Investment Sub-loans made under Part B.1 of the Project may be purchased at a reasonable price on the basis of the normal procurement procedures of the purchaser of such goods, works and services, account being taken also of other relevant factors such as time of delivery and efficiency and reliability of the goods and availability of maintenance facilities and spare parts therefor and, in the case of works and services, of their quality and the competence of the parties rendering them and, to the extent practicable, after evaluation and comparison from at least three suppliers or contractors.

Part C: Review by the Bank of Procurement Decisions

1. Review of invitations to bid and of proposed awards and final contracts:

(a) With respect to: (i) all contracts under Part A of this Schedule, and (ii) each of the first contract for goods or civil works awarded on the basis of local competitive bidding by each SWA, the procedures set forth in paragraphs 2 and 4 of Appendix 1 to the Guidelines shall apply. Where payments for such contract are to be made out of the Special Account, such procedures shall be modified to ensure that the two conformed copies of the contract required to be furnished to the Bank pursuant to said paragraph 2 (d) shall be furnished to the Bank prior to the making of the first payment out of the Special Account in respect of such contract.

(b) With respect to each contract not governed by the preceding paragraph, the procedures set forth in paragraphs 3 and 4 of Appendix 1 to the Guidelines shall apply. Where payments for such contract are to be made out of the Special Account, such procedures shall be modified to ensure that the two conformed copies of the contract together with the other information required to be furnished to the Bank pursuant to said paragraph 3 shall be furnished to the Bank as part of the evidence to be furnished pursuant to paragraph 4 of Schedule 5 to this Agreement.

(c) The provisions of the preceding subparagraphs (a) and (b) shall not apply to contracts on account of which the Bank has authorized withdrawals from the Loan Account on the basis of statements of expenditure. Such contracts shall be retained in accordance with Section 4.01 (c) (ii) of this Agreement.

2. The figure of 15% is hereby specified for purposes of paragraph 4 of Appendix 1 to the Guidelines.

Section II. Employment of Consultants

In order to assist the Borrower, the Guarantor, the SWAs and the Financial Intermediaries in carrying out the Project, the Borrower and the Guarantor shall employ, and the Borrower shall cause the SWAs and the Financial Intermediaries to employ, consultants whose qualifications, experience and terms and conditions of employment shall be satisfactory to the Bank. Such consultants shall be selected in accordance with principles and procedures satisfactory to the Bank on the basis of the "Guidelines for the use of Consultants by World Bank Borrowers and by the World Bank as Executing Agency" published by the Bank in August 1981.

SCHEDULE 5

Special Account

1. For the purposes of this Schedule:

(a) the term "Eligible Categories" means Categories (1) through (4) set forth in the table in paragraph 1 of Schedule 1 to this Agreement;

(b) the term "Eligible Expenditures" means expenditures in respect of the reasonable cost of goods and services required for the Project and to be financed out of the proceeds of the Loan allocated from time to time to the Eligible Categories in accordance with the provisions of Schedule 1 to this Agreement; and

(c) the term "Authorized Allocation" means an amount equivalent to one million dollars (\$1,000,000) to be withdrawn from the Loan Account and deposited in the Special Account pursuant to paragraph 3 of this Schedule.

2. Payments out of the Special Account shall be made exclusively for Eligible Expenditures in accordance with the provisions of this Schedule. The Borrower shall make withdrawals from the Special Account for payments of Eligible Expenditures on the basis of the evidence that the Bank shall have reasonably determined, and shall debit the Special Account with the amount in dollars so withdrawn or with the dollar equivalent of the currency other than dollars in which the payment was made, determined on the basis of the rate of exchange between the dollar and such currency in effect: (i) on the date each payment shall have been made, if the payment has taken place within 90 days before the date of the withdrawal in question has been requested; or (ii) on the date each withdrawal shall have been made.

3. After the Bank has received evidence satisfactory to it that the Special Account has been duly opened, 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 a deposit or deposits which do not exceed the aggregate amount of the Authorized Allocation. On the basis of such request or requests, the Bank shall, on behalf of the Borrower, withdraw from the Loan Account and deposit in the Special Account such amount or amounts as the Borrower shall have requested.

(b) (i) For replenishment of the Special Account, the Borrower shall furnish to the Bank requests for deposits into the Special Account at such intervals as the Bank shall specify.

(ii) 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 paragraph 4 of this Schedule for the payment or payments in respect of which replenishment is requested. On the

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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 made out of the Special Account for eligible expenditures. All such deposits shall be withdrawn by the Bank from the Loan Account under the respective eligible Categories, and in the respective equivalent amounts, as shall have been justified by said documents and other evidence.

4. 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.

5. Notwithstanding the provisions of paragraph 3 of this Schedule, the Bank shall not be required to make further deposits into the Special Account:

(a) if, at any time, the Bank shall have determined that all further withdrawals should be made by the Borrower directly from the Loan Account in accordance with the provisions of Article V of the General Conditions and paragraph (a) of Section 2.02 of this Agreement; or

(b) once the total unwithdrawn amount of the Loan allocated to the Eligible Categories less the amount of any outstanding special commitment entered into by the Bank pursuant to Section 5.02 of the General Conditions with respect to the Project, 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 allocated to the Eligible Categories 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.

6. (a) If the Bank shall have determined at any time that any payment out of the Special Account: (i) was made for an expenditure or in an amount not eligible pursuant to paragraph 2 of this Schedule; or (ii) was not justified by the evidence furnished to the Bank, the Borrower shall, promptly upon notice from the Bank: (A) provide such additional evidence as the Bank may request; or (B) 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 or the portion thereof not so eligible or justified. 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 shall have determined at any time that any amount outstanding in the Special Account will not be required to cover further payments for eligible expenditures, 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 paragraphs 6 (a), (b) and (c) of this Schedule shall be credited to the Loan Account for subsequent withdrawal or for cancellation in accordance with the relevant provisions of this Agreement, including the General Conditions.

SCHEDULE 6

Terms and Conditions of
Subsidiary Loans

1. Repayment Term. Subsidiary Loans shall have an amortization period not to exceed seventeen years, including a maximum grace period of five years.

2. Interest Rate. The interest rate on Subsidiary Loans shall be set and readjusted in accordance with the provisions of the General Interest Rate Agreement.

3. Currency. Subsidiary Loans shall be made and repaid in pesos.

4. Specific Terms and Conditions. Each Subsidiary Loan shall be made pursuant to a written Subsidiary Loan Agreement between the Borrower, as party of the first part, and the SWA and the Eligible State, as parties of the other, on terms and conditions satisfactory to the Bank, including, inter alia, specific provisions establishing the following obligations of the SWA and the Eligible State:

I. Obligations of the SWA

(a) Performance Standards. Carry out the Sub-project with due diligence and efficiency and in conformity with appropriate technical, administrative, financial and environmental standards and practices.

(b) Procurement. Procure goods, works and services required for the carrying out of the relevant Sub-project in accordance with the provisions of Schedule 4 to this Agreement, such goods, works and services to be used exclusively for the carrying out of such Sub-project.

(c) Records and Accounts. Maintain separate Sub-project records and accounts adequate to reflect, in accordance with sound accounting practices, the operations, resources, and expenditures with respect to the Sub-project.

(d) Auditing. (i) have the records and accounts referred to in sub-paragraph (c) above for each fiscal year audited in accordance with generally accepted auditing standards and procedures consistently applied, by independent and qualified auditors; (ii) furnish to the Borrower and the Bank as soon as available, but in any case not later than six months after the end of each such year: (A) certified copies of the records and accounts so audited, and (B) the report of such audit by said auditors, of such scope and in such detail as the Bank shall have reasonably requested; and (iii) furnish to the Borrower and the Bank such other information concerning said records and accounts as well as the audit thereof as the Borrower or the Bank shall reasonably request.

(e) Statements of Expenditure. (i) Maintain separate records and accounts in accordance with sub-paragraph (c) above, reflecting all expenditures with respect to which withdrawals from the Loan Account were made on the basis of statements of expenditure; (ii) retain, until at least one 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 representatives of the Borrower and the Bank to examine such records and accounts; and (iv) ensure that such separate records are included in the annual audit referred to in sub-paragraph (d) above and that the report thereof contains, in respect of such separate accounts, a separate opinion by said auditors as to whether the statement of expenditures 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.

(f) Annual Water Plan. Prepare and submit to SPS for its approval proposed Annual Water Plan and, after obtaining such approval, furnish such Plan to the Borrower and the Bank for the Bank's review and comment, by no later than September 30 of each year, including exchanging views with the Bank on such Plan and the progress in implementing such Plan during previous years.

(g) Supervision. Carry out supervision of the Sub-project, in a manner satisfactory to the Borrower and the Bank, through the Eligible State.

(h) Tariffs. Set and maintain in the communities in which Sub-projects are carried out a level of tariff as shall be required by the SWA to obtain in each calendar year revenues sufficient to cover the sum of: (i) all of its operating and maintenance expenses; and (ii) debt service requirements on the Subsidiary Loans.

(i) Consultants. Employ consultants, satisfactory to the Bank, to carry out the technical assistance and training under Part A.3 of the Project.

II. Obligations of the Eligible State

(a) Monitoring. Carry out monitoring, coordination and evaluation of Sub-projects in a manner satisfactory to the Borrower and the Bank, with staff adequate in numbers, qualification and experience.

(b) Guarantee. Guarantee (i) the payment of principal, interest and other charges on the Subsidiary Loan to the Borrower; and (ii) the punctual performance by the SWA of all other obligations under the Subsidiary Loan Agreement.

(c) Counterpart Funds. Provide counterpart financing for the Sub-projects in the form of funds, infrastructure, materials, and labor and any other resources as may be required to carry out the Sub-projects and achieve the objectives of the Project.

(d) Annual Water Plan. Through its SPS review and approve the proposed Annual Water Plan.

5. Other Terms. Each Subsidiary Loan Agreement shall also include the Borrower's right to:

(a) Inspection and Records. Inspect, by itself or jointly with representatives of the Bank, if the Bank shall so request, the goods and the sites, works, and construction included in the Sub-project, the operation thereof, and any relevant records and documents;

(b) Information. Obtain from the SWAs and the Eligible State all such information as the Borrower or the Bank, through the Borrower, shall reasonably request related to the foregoing provisions of the Subsidiary Loan Agreement; and

(c) Suspension and Termination. Suspend or terminate the right of the SWAs to use the proceeds of the Subsidiary Loan upon failure by the SWA or the Eligible State, to perform any of their obligations under the Subsidiary Loan Agreement, or upon notice by the Bank that it intends to exercise its remedies under Article V of the Loan Agreement.

SCHEDULE 7

Terms and Conditions of Participation Agreements

Section I: General Terms

1. Each Participation Agreement shall be made pursuant to a written agreement between the Borrower, as party of the first part, and the Financial Intermediary and the Eligible State, as parties of the other, on terms and conditions satisfactory to the Bank, providing arrangements for, inter alia:

(a) relending a portion of the proceeds of the Loan to such Financial Intermediary for purposes of making Investment Subloans under the Project, but only on condition that such Financial Intermediary agrees to be bound by the terms and conditions of this Agreement regarding its obligations in the execution of the Project, including, without limitation, Section 4.01 of this Agreement (maintenance of records and accounts), and Schedule 4 to this Agreement (procurement), as the same may be amended from time to time by agreement between the Borrower and the Bank;

(b) repayment to the Borrower, of all amounts relented to the Financial Intermediary; such Financial Intermediary to bear the credit risk associated with any failure by Project Beneficiaries to repay Investment Subloans;

(c) the requirement that all Investment Subloans financed under the Project shall be made in accordance with the terms and conditions of Schedule 8 to this Agreement;

(d) the requirement that such Financial Intermediary furnish to the Bank, through the Borrower, such information as the Borrower may require to comply with its obligations under this Agreement;

(e) the requirement that the Financial Intermediary submit, through the Borrower, to the Bank for its prior approval, each Investment Subloan for a principal amount equivalent to fifty thousand dollars (US\$50,000) or more, that the Financial Intermediary submit to the Borrower, for its prior approval, each Investment Subloan for a principal amount equivalent to fifteen thousand dollars (US\$15,000) or more, and that the Financial Intermediary shall have the sole right of approval for Subloans below such amount;

(f) the requirement that the Financial Intermediary ensure that Investments do not result in any negative environmental impact; and

(g) the right of the Borrower to suspend or terminate the right of the Financial Intermediary to use the proceeds of the Loan upon failure by such Financial Intermediary or the relevant Eligible State to perform any of their obligations under the Participation Agreement, or upon notice by the Bank that it intends to exercise its remedies under Article V of the Loan Agreement.

2. The Borrower shall cause each Financial Intermediary to exercise its rights in relation to each Investment Subloan, Project Beneficiary and Investment in such manner as to: (i) protect the interests of the Borrower, the Bank, the Financial Intermediary and the Eligible State; (ii) comply with its obligations under this Agreement; and (iii) achieve the purposes of the Project.

3. The Borrower shall cause each Financial Intermediary, except FIMINSSE, as a Promotion Agency: (i) to promote the Investments in communities in the Eligible State, including mobilizing community support; (ii) to maintain an adequate level of extension workers; and (iii) to identify Investments, prepare feasibility studies, and train Project Beneficiaries in the skills require to carry out such Investments.

4. The Borrower shall cause each Financial Intermediary, except FIMINSSE, as a Promotion Agency, to employ consultants, satisfactory to the Bank, to carry out the technical assistance program under Part B.2 of the Project.

Section II: Terms of Relending the Proceeds of the Loan

Amounts relent by the Borrower to a Financial Intermediary shall be in accordance with the following terms and conditions:

(a) Repayment Term. All amounts relent by the Borrower to a Financial Intermediary pursuant to a Participation Agreement shall be repaid over the same term as the Investment Subloan(s) made by the Financial Intermediary utilizing such amounts.

(b) Interest Rate. The interest rate shall be the interest rate for the Investment Subloan, minus a financial intermediation margin of up to 4.5 percentage points.

(c) Currency. All amounts relent by the Borrower to a Financial Intermediary shall be made and repaid in pesos.

Section III: Specific Obligations of the Eligible States

Each Participation Agreement shall contain, inter alia, the following specific provisions establishing the Eligible State's obligations to:

(a) Guarantee. Guarantee (i) the payment of principal, interest and other charges on the Investment Subloan to the Borrower; and (ii) the punctual performance by the Financial Intermediary of all other obligations under the Participation Agreement.

(b) Counterpart Funds. Provide counterpart financing for the Investments in the form of funds, infrastructure, materials, and labor and any other resources as may be required to carry out the Investment and achieve the objectives of the Project.

(c) Promotion. In the State of Queretaro only, the obligation of such State through IDEAS, as a Promotion Agency: (i) to promote the Investments in communities, including mobilizing community support, and for such purposes to employ consultants; (ii) to maintain an adequate level of extension workers; and (iii) to identify Investments, prepare feasibility studies, and train Project Beneficiaries in the skills required to carry out such Investments.

(d) Consultants. In the case of the State of Queretaro only, the obligation of such State through IDEAS, as a Promotion Agency, to employ consultants, satisfactory to the Bank, to carry out the technical assistance program under Part B.2 of the Project.

SCHEDULE 8

Terms and Conditions of
Investment Subloans

1. Terms and Conditions

Each Investment Subloan, unless otherwise agreed by the Bank, shall include the following terms and conditions:

- (i) Appraisal. Each Investment Subloan shall be made only for an Investment appraised by the Financial Intermediary making such Investment Subloan;
- (ii) Currency. Investment Subloans shall be made and repaid in pesos;
- (iii) Term. Investment Subloans may be made for a term of up to twelve years and may include a grace period not exceeding three years;
- (iv) Interest Rate. The interest rate on Investment Subloans shall be set and readjusted in accordance

with the provisions of the General Interest Rate Agreement;

- (v) Maximum Amount Limitations. (i) the maximum amount of each Investment Subloan shall be the equivalent of US\$1,000 in the case of individual Project Beneficiaries but shall not in the aggregate exceed US\$3,000 per individual Project Beneficiary and US\$3,000 equivalent per member in the case of groups or entities that qualify as Project Beneficiaries; and
- (vi) Training. Each Investment Subloan shall be made only after the relevant Promotion Agency certifies that the training needs have been identified and adequate training plans have been prepared for Project Beneficiaries.

2. Written Contract. Each Investment Subloan financing an Investment shall be made pursuant to a written contract between the Financial Intermediary and the Project Beneficiary providing:

- (i) for the obligation of such Project Beneficiary, to carry out and operate the Investment with due diligence and efficiency and in accordance with the standards and practices referred to in Section 3.01 of this Agreement;
 - (ii) that the goods, works and services to be financed out of the proceeds of the Loan shall be procured in accordance with the provisions of Part B.4 of Schedule 4 to this Agreement;
 - (iii) that the goods and works to be financed out of the proceeds of the Loan shall be used exclusively in the carrying out of the Investment;
 - (iv) that the Financial Intermediary can inspect, by itself or jointly with representatives of the Borrower, and the Bank, if the Borrower, or the Bank shall so request, such goods and the sites, works, plants and construction included in the Investment, the operation thereof, and any relevant records and documents;
 - (v) for the obligation of the Project Beneficiary to furnish all such information as the Borrower or the Bank or the Financial Intermediary shall reasonably request relating to the foregoing and to the administration, operations and financial condition of the Project Beneficiary and to the benefits to be derived from the Investment Sub-project; and
 - (vi) the right of the Financial Intermediary to suspend or terminate the right of the Project Beneficiary to the use of the proceeds of the Investment Subloan upon failure by such Project Beneficiary to perform any of their obligations under the contract with the Financial Beneficiary or upon notice by the Bank that it intends to exercise its remedies under Article V of the Loan Agreement.
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