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CREDIT NUMBER 4872-IN

Project Agreement

(Kerala Local Government and Service Delivery Project)

between

INTERNATIONAL DEVELOPMENT ASSOCIATION

and

STATE OF KERALA

Dated July 4, 2011

PROJECT AGREEMENT

AGREEMENT dated July 4, 2011, entered into between INTERNATIONAL DEVELOPMENT ASSOCIATION (“Association”) and STATE OF KERALA (“Project Implementing Entity”) (“Project Agreement”) in connection with the Financing Agreement (“Financing Agreement”) of same date between India (“Recipient”) and the Association. The Association and the Project Implementing Entity hereby agree as follows:

ARTICLE I — GENERAL CONDITIONS; DEFINITIONS

- 1.01. The General Conditions (as defined in the Appendix to the Financing Agreement) constitute an integral part of this Agreement.
- 1.02. Unless the context requires otherwise, the capitalized terms used in this Agreement have the meanings ascribed to them in the Financing Agreement or the General Conditions.

ARTICLE II — PROJECT

- 2.01. The Project Implementing Entity declares its commitment to the objectives of the Project. To this end, the Project Implementing Entity shall carry out the Project in accordance with the provisions of Article IV of the General Conditions, and shall provide promptly as needed, the funds, facilities, services and other resources required for the Project.
- 2.02. Without limitation upon the provisions of Section 2.01 of this Agreement, and except as the Association and the Project Implementing Entity shall otherwise agree, the Project Implementing Entity shall carry out the Project in accordance with the provisions of the Schedule to this Agreement.

ARTICLE III — REPRESENTATIVE; ADDRESSES

- 3.01. The Project Implementing Entity’s Representative is any of the following: Chief Secretary, Principal Secretary, Secretary, or Additional Secretary of the Local Self Government Department.
- 3.02. The Association’s Address is:

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

Facsimile:

1-202-477-6391

3.03. The Project Implementing Entity's Address is:

Local Self Government Department
4th Floor, Secretariat
Thiruvanthapuram
Kerala 695001

Facsimile: 0471 2327395

AGREED at Thiruvanthapuram, India, as of the day and year first above written.

INTERNATIONAL DEVELOPMENT ASSOCIATION

By /s/ Roland Lomme
Authorized Representative

STATE OF KERALA

By /s/ James Varghese
Authorized Representative

SCHEDULE

Execution of the Project

Section I. Implementation Arrangements

A. Institutional Arrangements

1. The Project Implementing Entity shall carry out the Project through the PMU, and, in the carrying out of Parts B, C and D of the Project, shall specifically use the services of the Implementing Agencies under MOUs, in form and substance agreed with the Association, that shall, among other things, detail the obligations of each party to the MOU.
2. The Project Implementing Entity shall provide Performance Grants to Participating GPs and Participating Municipalities to carry out Sub-projects in accordance with the objectives, policies, procedures, time schedules and other provisions set forth in the PIM and the ESMF, and shall not amend or waive any provisions of the PIM, ESMF and Tribal and Other Vulnerable Group Development Framework, without the prior mutual agreement between the Project Implementing Entity and the Association.
3. Throughout the duration of the Project, the Project Implementing Entity shall: (i) make adequate budgetary allocation for timely release of Performance Grants to Participating GPs and Participating Municipalities; (ii) ensure that Performance Grants are transferred to Participating GPs and Participating Municipalities in a timely manner; and (iii) cause Participating GPs and Participating Municipalities to maintain policies and procedures adequate to monitor and evaluate on an ongoing basis, in accordance with the systems and indicators detailed in the PIM, the carrying out of the Sub-projects and the achievement of the objectives thereof.
4. The Project Implementing Entity shall cause each of the Participating GPs and Participating Municipalities to carry out Sub-projects in accordance with its planning guidelines, and shall provide periodic evidence to the Association of progress achieved in the implementation of Sub-projects in accordance with indicators agreed with the Association.
5. The Project Implementing Entity shall ensure that no works shall be carried out under the Project, including any Sub-project that may result in the involuntary resettlement of local population.

6. The Project Implementing Entity shall, no later than six (6) months after the Effective date, appoint support engineers, with suitable qualifications and experience, to join the LSGD.
7. The Project Implementing Entity undertakes that, until completion of the Project, the total annual budgeted State Finance Commission award amount for local self governments shall not decrease in real terms, as measured using the national inflation rate as deflator and using 2010/2011 as the base year.
8. Throughout the duration of the Project, the Project Implementing Entity shall:
 - (a) at the Project State level:
 - (i) maintain the PMU and ensure that:
 - (A) it is responsible for overseeing the progress of the activities financed under the Project, including their design, implementation and maintenance; and
 - (B) it has an adequate organizational structure with functions, powers, staff and resources necessary and appropriate to carry out its responsibilities under the Project;
 - (ii) cause the PMU to carry out its responsibilities under the Project, including: (i) ensuring timely Sub-project implementation, as provided for in the PIM; (ii) preparing annual work programs, budgets, annual procurement plans and providing quality control; (iii) preparing withdrawal applications for submission to the Association; (iv) maintaining consolidated Project accounts and ensuring that Project audits are carried out in a timely manner and pursuant to the standard terms of reference; (v) preparing six-monthly Interim Unaudited Financial Reports, information on financial execution, reports on Project implementation progress, as well as procurement reports; and (vi) ensuring proper implementation of the ESMF by the GPs and Municipalities.
 - (b) maintain coordination units, mentoring teams and training centers with an adequate organizational structure, staff and resources necessary and appropriate to carry out their responsibilities under the Project.
9. The Project Implementing Entity shall take all necessary steps to:
 - (a) ensure that the Participating GPs and Participating Municipalities carry out their respective Project implementation responsibilities in accordance

with the Governance and Accountability Action Plan, the Project Implementation Manual, the Procurement Manual and the Procurement Plan; and

- (b) ensure that: (i) the provisions of the manuals and plans referred to in sub-paragraph (a) above are not revised, amended or abrogated without the prior mutual agreement between the Project Implementing Entity and the Association; and (ii) no action is taken which shall prevent or interfere with the implementation of said Manuals or Plans.

B. Performance Grant Access Criteria and Performance Measures

- 1. To be eligible for a Performance Grant, a Participating GP and a Participating Municipality shall have:

- (i) For the first year (2011/12):
 - (a) received an audit opinion from the Project State's local fund auditor for financial year 2008/2009, which is not adverse, and includes no disclaimers or observations that affect the integrity of the annual financial statements of the GP/Municipality, and/or indicate significant weaknesses in financial management and/or accounting; and
 - (b) passed, by March 31, the annual budget for the forthcoming year, with a copy availed to LSGD by April 30, 2012;
- (ii) For the second year:
 - (a) passed, by March 31, the annual budget for the forthcoming year, with a copy availed to LSGD by April 30;
 - (b) received an audit opinion from the Project State's local fund auditor for financial years 2009/2010 and 2010/2011, which is not adverse, and includes no disclaimers or observations that affect the integrity of the annual financial statements of the GP/Municipality, and/or indicate significant weaknesses in financial management and/or accounting; and
 - (c) submitted an annual plan for financial year 2011/12 to the Project State, approved by both the GP or Municipality and the district planning committee, and a copy availed to LSGD;
- (iii) For the subsequent years:

- (a) passed, by March 31, the annual budget for the forthcoming year, with a copy availed to LSGD by April 30; and
- (b) met the performance requirements of an annual independent assessment based on the criteria specified in the PIM.

C. Resolution

1. For purposes of Part A of the Project, the Project Implementing Entity, through the PMU, shall make arrangements, agreed with the Association, to define the relationship with each Participating GP and Participating Municipality with respect to this Project, whereby the Project State shall agree to provide to such Participating GP or Participating Municipality a Performance Grant, on terms and conditions agreed with the Association, including details of disbursement schedules and procurement procedures, details of safeguards policies to be carried out as may be needed for the management of the environment, and the following additional terms and conditions:
 - (a) require the Participating GP/Municipality to carry out all Sub-project activities with due diligence and efficiency and in accordance with sound technical, financial, managerial and environmental standards and practices, and maintain adequate records;
 - (b) obtain all such information as the Association or the Recipient shall reasonably request; and
 - (c) suspend or terminate the right of a Participating GP/Municipality to the use of the proceeds of the Credit upon failure by such GP or Municipality to perform its obligations under the Resolution.

D. Advance and Release of Performance Grants

1. Proceeds of the Credit advanced for the Performance Grants shall be released by the Association annually, provided that the Project Implementing Entity has furnished to the Association:
 - (a) for FY 2011/2012:
 - (i) initial cash flow forecasts for FY 2011/2012 for Performance Grants; and
 - (ii) PMU's certification of receipt, from all Participating GPs and Participating Municipalities, of the legal instrument referred to in paragraph C.1, Section I, of this Schedule;

- (b) for FY 2012/2013:
 - (i) initial cash flow forecasts for FY 2012/2013 for Performance Grants;
 - (ii) a detailed schedule of funds released by the Project State to the Participating GPs and Participating Municipalities under Performance Grants during the previous Fiscal Year, including the release dates thereof;
 - (iii) receipt, from Participating GPs and Participating Municipalities of the legal instrument referred to in paragraph C.1, Section I, of this Schedule; and
 - (iv) PMU's certification to the effect that there have been no significant reallocations, deviations or suspension of funding to any Participating GP or Participating Municipality in the previous year;
- (c) for each of the subsequent FYs:
 - (i) an initial cash flow forecast for the forthcoming Fiscal Year for Performance Grants;
 - (ii) a detailed schedule of funds released by the Project State to the Participating GPs and Participating Municipalities for Performance Grants during the previous Fiscal Year, and amounts to be released in the following Fiscal Year, including the date of each such release;
 - (iii) PMU's certification to the effect that there have been no significant reallocations, deviations or suspension of funding to any Participating GP or Participating Municipality in the previous year; and
 - (iv) receipt of the legal instrument referred to in paragraph C.1, Section I, of this Schedule in respect of any and all first time Participating GPs or Participating Municipalities.

E. Anti-Corruption

The Project Implementing Entity shall ensure that the Project, including all Sub-projects, shall be carried out in accordance with the provisions of the Anti-Corruption Guidelines and those of the GAAP.

F. Environmental and Social Safeguards Management

1. The Project Implementing Entity shall, in carrying out the Project, apply and implement, and, in the case of Sub-projects, cause to be applied and implemented:
 - (a) the Environmental and Social Management Framework and the environmental management plans prepared pursuant to the provisions of said framework; and
 - (b) the Tribal and Other Vulnerable Group Development Framework, and the plans prepared pursuant to the provisions of said framework;

all in a manner and substance agreed with the Association.

Section II. Project Monitoring, Reporting and Evaluation**A. Project Reports**

1. The Project Implementing Entity shall monitor and evaluate the progress of the Project and prepare Project Reports in accordance with the provisions of Section 4.08 of the General Conditions and on the basis of indicators agreed with the Association. Each such Project Report shall cover the period of six (6) months of the Recipient's financial year, and shall be furnished to the Association not later than forty-five (45) days after the end of said period.
2. The performance indicators referred to in sub-paragraph 1 above shall consist of the following: (i) seventy percent (70%) of the GPs and Municipalities shall have passed the performance assessments for well-functioning fiduciary, planning and service delivery systems; (ii) a well established performance-based grant system is increasingly financed by the Project State; and (iii) the number of direct Project beneficiaries, of which a certain percentage are female.
3. Without limitation to the provision of sub-paragraph 1 above, the Project Implementing Entity shall, not later than thirty (30) months after the Effective Date, carry out jointly with the Association a midterm review, which shall cover, among other things: (i) the performance by Participating GPs and Participating Municipalities under Part A of the Project; (ii) progress in meeting the Project's objectives; and (iii) overall Project performance as measured against the performance indicators referred to in sub-paragraph 1 above. Thereafter, the Project Implementing Entity shall take all measures required to ensure the efficient completion of the Project and the achievement of the objectives thereof, based on the conclusions and recommendations of the said mid-term review.

B. Financial Management, Financial Reports and Audits

1. The Project Implementing Entity shall maintain a financial management system and prepare Project's Financial Statements in accordance with consistently applied accounting standards acceptable to the Association, both in a manner adequate to reflect the operations, resources, expenditures and financial condition of the Project.
2. Without limitation on the provisions of Part A of this Section, the Project Implementing Entity shall prepare and furnish to the Association not later than forty-five (45) days after the end of each semester, Interim Unaudited Financial Reports (IUFs) for the Project covering the semester, in form and substance satisfactory to the Association.
3. The Project Implementing Entity shall have the Project's Financial Statements referred to above audited by independent auditors acceptable to the Association, in accordance with consistently applied auditing standards acceptable to the Association. Each audit of these financial statements shall cover the period of one (1) financial year of the Recipient. The audited financial statements for each period shall be furnished to the Association not later than six (6) months after the end of the period.

Section III. Procurement

A. General

1. **Goods and Works.** All goods and works required for the Project, and to be financed out of the proceeds of the Financing shall be procured in accordance with the requirements set forth or referred to in Section I of the Procurement Guidelines, and with the provisions of this Section.
2. **Consultants' Services.** All consultants' services required for the Project and to be financed out of the proceeds of the Financing shall be procured in accordance with the requirements set forth or referred to in Sections I and IV of the Consultant Guidelines, and with the provisions of this Section.
3. **Definitions.** The capitalized terms used below in this Section to describe particular procurement methods or methods of review by the Association of particular contracts, refer to the corresponding method described in the Procurement Guidelines, or Consultant Guidelines, as the case may be.

B. Particular Methods of Procurement of Goods and Works

1. **International Competitive Bidding.** Except as otherwise provided in paragraph 2 below, goods and works shall be procured under contracts awarded on the basis of International Competitive Bidding, subject to the following additional procedures, namely, that Standard Bidding Documents and Procedures approved by the Association shall be used. The Procurement Plan shall specify the circumstances under which such method may be used.
2. **Other Methods of Procurement of Goods and Works.** The following table specifies the methods of procurement, other than International Competitive Bidding, which may be used for goods and works for Parts B, C and D of the Project. The Procurement Plan shall specify the circumstances under which such methods may be used:

Procurement Method	
(a)	National Competitive Bidding, subject to the additional conditions set forth in the Procurement Manual, the Procurement Plan, and other provisions agreed upon from time to time between the Project State and the Association
(b)	Shopping
(c)	Direct Contracting

C. Procurement of Goods and Works under Part A

All goods and works required for Part A of the Project shall be procured by the Participating GPs and Participating Municipalities in accordance with the provisions of the Procurement Manual.

D. Particular Methods of Procurement of Consultants’ Services

1. **Quality- and Cost-based Selection.** Except as otherwise provided in paragraph 2 below, consultants’ services shall be procured under contracts awarded on the basis of Quality- and Cost-based Selection, subject to the following additional procedures, namely, that Standard Request for Proposal and Procedures approved by the Association shall be used. The Procurement Plan shall specify the circumstances under which such method may be used.
2. **Other Methods of Procurement of Consultants’ Services.** The following table specifies methods of procurement, other than Quality- and Cost-based Selection, which may be used for consultants’ services. The Procurement Plan shall specify the circumstances under which such methods may be used.

Procurement Method
(a) Quality-Based Selection
(b) Fixed Budget Selection
(c) Selection based on Consultants' Qualifications
(d) Single Source Selection
(e) Least Cost Selection
(f) Selection of Individual Consultants

E. Review by the Association of Procurement Decisions

The Procurement Plan shall set forth those contracts which shall be subject to the Association's Prior Review. All other contracts shall be subject to Post Review by the Association as per the Procurement Plan for contracts under Parts B, C and D, and as per the Procurement Manual for contracts under Part A.