

CONFORMED COPY

CREDIT NUMBER 3293 NEP

Development Credit Agreement

(Road Maintenance and Development Project)

between

KINGDOM OF NEPAL

and

INTERNATIONAL DEVELOPMENT ASSOCIATION

Dated December 22, 1999

CREDIT NUMBER 3293 NEP

DEVELOPMENT CREDIT AGREEMENT

AGREEMENT, dated December 22, 1999, between KINGDOM OF NEPAL (the Borrower) and INTERNATIONAL DEVELOPMENT ASSOCIATION (the Association).

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

(B) the Association has agreed, on the basis, inter alia, of the foregoing, to extend the credit provided for in Article II of this Agreement (the Credit) 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 Development Credit Agreements" of the Association, dated January 1, 1985 (as amended through December 2, 1997) (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) "DOR" means the Department of Roads of the Borrower within MOWT (as hereinafter defined);

(b) "EIA" means the Environmental Impact Assessment of the Borrower dated August 19, 1999 and approved by the Association, setting forth, inter alia, the assessment of environmental impacts of the construction of new roads under the Project and recommendations for mitigation of adverse impacts and enhancement of positive impacts based on such assessment;

(c) "Eligible Categories" means categories (1), (2) and (3) set forth in the table in Part A.1 of Schedule 1 to this Agreement;

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

(e) "EMAP" means each of (i) the Environmental Management Action Plan based on and resulting from the EIA, dated August 19, 1999 and approved by the Association, setting forth, inter alia, the measures to mitigate adverse environmental impacts and enhance positive environmental impacts of the construction of new roads under the Project, (ii) the Environmental Management Action Plan based on and resulting from the IEE (as hereinafter defined) for the upgrading of roads under the Project, dated July 28, 1999 and approved by the Association, setting forth, inter alia, the measures to mitigate adverse environmental impacts and enhance positive environmental impacts of the upgrading of roads under the Project and (iii) the Environmental Management Action Plan based on and resulting from the IEE for the rehabilitation of roads under the Project, dated August 19, 1999 and approved by the Association, setting forth, inter alia, the measures to mitigate adverse environmental impacts and enhance positive environmental impacts of the rehabilitation of roads under the Project;

(f) "Fiscal Year" or "FY" means the fiscal year of the Borrower, which begins approximately on July 16 of a calendar year and ends approximately on July 15 of the following calendar year;

(g) "IEE" means each of (i) the Initial Environmental Examination of the Borrower dated July 28, 1999 and approved by the Association, setting forth, inter alia, the assessment of environmental impacts of the upgrading of roads under the Project and recommendations for mitigation of adverse impacts and enhancement of positive impacts based on such assessment and (ii) the Initial Environmental Examination of the Borrower dated August 19, 1999 and approved by the Association, setting forth, inter alia, the assessment of environmental impacts of the rehabilitation of roads under the Project and recommendations for mitigation of adverse impacts and enhancement of positive impacts based on such assessment;

(h) "MOWT" means the Ministry of Works and Transport of the Borrower;

(i) "Nepal Rastra Bank" means the central bank of the Borrower, established and operating pursuant to the Nepal Rastra Bank Act, 2012 (1955), as amended from time to time;

(j) "Nepalese Rupees" or "NRs" means the currency of the Borrower;

(k) "PCU" means the Project Coordination and Implementation Unit established in the DOR and responsible for, inter alia, the planning, implementation, coordination and management of supervision and monitoring and evaluation of activities to be carried out under the Project;

(l) "Priority Investment Plan" means the Priority Investment Plan for the Road Sector (February 1997) of the Borrower, setting forth, inter alia, objectives, policies and actions to undertake priority projects for sustainable development of the strategic and rural road network for the period 1997-2006;

(m) "Project Implementation Plan" means the Project Implementation Plan of the Borrower for the carrying out of the Project, dated September 1999 and approved by the Association, as the same may be updated from time to time with the agreement of the Association;

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

(o) "Project Preparation Advance" means the project preparation advance granted by the Association to the Borrower pursuant to the letter agreement signed on behalf of the Association on August 28, 1998 and on behalf of the Borrower on November 18, 1998;

(p) "RAP" means the Resettlement Action Plan of the Borrower dated June 1999 and the Addendum thereto dated July 1999, both approved by the Association, setting forth, inter alia, the entitlement framework, institutional arrangements, implementation schedules, monitoring mechanisms and cost estimates for the resettlement and rehabilitation of people affected by the implementation of the Project;

(q) "Roads Board" means a joint public and private sector board proposed to be established by the Borrower for the purpose of overseeing the management of the maintenance of the strategic, urban and rural road network and financial allocations for maintenance in the road sector;

(r) "Road Fund" means a fund proposed to be established by the Borrower and managed by the Roads Board and comprising various sources including a portion of road user revenues earmarked for financing a portion of road maintenance requirements, including routine, recurrent, periodic and emergency maintenance operations; and

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

ARTICLE II

The Credit

Section 2.01. The Association agrees to lend to the Borrower, on the terms and conditions set forth or referred to in this Agreement, an amount in various currencies equivalent to forty million one hundred thousand Special Drawing Rights (SDR 40,100,000).

Section 2.02. (a) The amount of the Credit may be withdrawn from the Credit Account in accordance with the provisions of Schedule 1 to this Agreement for expenditures made (or, if the Association shall so agree, to be made) in respect of the reasonable cost of goods and services required for the Project and to be financed out of the proceeds of the Credit.

(b) Promptly after the Effective Date, the Association shall, on behalf of the Borrower, withdraw from the Credit Account and pay to itself the amount required to repay the principal amount of the Project Preparation Advance withdrawn and outstanding as of such date and to pay all unpaid charges thereon. The unwithdrawn balance of the authorized amount of the Project Preparation Advance shall thereupon be canceled.

Section 2.03. The Closing Date shall be December 31, 2004 or such later date as the Association shall establish. The Association shall promptly notify the Borrower of such later date.

Section 2.04. (a) The Borrower shall pay to the Association a commitment charge on the principal amount of the Credit not withdrawn from time to time at a rate to be set by the Association as of June 30 of each year, but not to exceed the rate of one-half of one percent (1/2 of 1%) per annum.

(b) The commitment charge shall accrue: (i) from the date sixty days after the date of this Agreement (the accrual date) to the respective dates on which amounts shall be withdrawn by the Borrower from the Credit Account or canceled; and (ii) at the rate set as of the June 30 immediately preceding the accrual date and at such other rates as may be set from time to time thereafter pursuant to paragraph (a) above. The rate set as of June 30 in each year shall be applied from the next date in that year specified in Section 2.06 of this Agreement.

(c) The commitment charge shall be paid: (i) at such places as the Association shall reasonably request; (ii) without restrictions of any kind imposed by, or in the territory of, the Borrower; and (iii) in the currency specified in this Agreement for the purposes of Section 4.02 of the General Conditions or in such other eligible currency or currencies as may from time to time be designated or selected pursuant to the provisions of that Section.

Section 2.05. The Borrower shall pay to the Association a service charge at the rate of three-fourths of one percent ($3/4$ of 1%) per annum on the principal amount of the Credit withdrawn and outstanding from time to time.

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

Section 2.07. (a) Subject to paragraphs (b), (c) and (d) below, the Borrower shall repay the principal amount of the Credit in semiannual installments payable on each March 15 and September 15 commencing March 15, 2010 and ending September 15, 2039. Each installment to and including the installment payable on September 15, 2019 shall be one percent (1%) of such principal amount, and each installment thereafter shall be two percent (2%) of such principal amount.

(b) Whenever: (i) the Borrower's per capita gross national product (GNP), as determined by the Association, shall have exceeded for three consecutive years the level established annually by the Association for determining eligibility to access the Association's resources; and (ii) the Bank shall consider the Borrower creditworthy for Bank lending, the Association may, subsequent to the review and approval thereof by the Executive Directors of the Association and after due consideration by them of the development of the Borrower's economy, modify the repayment of installments under paragraph (a) above by: (A) requiring the Borrower to repay twice the amount of each such installment not yet due until the principal amount of the Credit shall have been repaid; and (B) requiring the Borrower to commence repayment of the principal amount of the Credit as of the first semiannual payment date referred to in paragraph (a) above falling six months or more after the date on which the Association notifies the Borrower that the events set out in this paragraph (b) have occurred, provided, however, that there shall be a grace period of a minimum of five years on such repayment of principal.

(c) If so requested by the Borrower, the Association may revise the modification referred to in paragraph (b) above to include, in lieu of some or all of the increase in the amounts of such installments, the payment of interest at an annual rate agreed with the Association on the principal amount of the Credit withdrawn and outstanding from time to time, provided that, in the judgment of the Association, such revision shall not change the grant element obtained under the above-mentioned repayment modification.

(d) If, at any time after a modification of terms pursuant to paragraph (b) above, the Association determines that the Borrower's economic condition has deteriorated significantly, the Association may, if so requested by the Borrower, further modify the terms of repayment to conform to the schedule of installments as provided in paragraph (a) above.

Section 2.08. The currency of the United States of America is hereby specified for the purposes of Section 4.02 of the General Conditions.

ARTICLE III

Execution of the Project

Section 3.01. (a) The Borrower declares its commitment to the objectives of the Project, and, to this end, shall carry out the Project, through DOR with the assistance of MOWT, with due diligence and efficiency and in conformity with appropriate administrative, financial, engineering, transport and environmental practices, and shall provide, promptly as needed, the funds, facilities, services and other resources required for the Project.

(b) Without limitation upon the provisions of paragraph (a) of this Section and except as the Borrower and the Association shall otherwise agree, the Borrower

shall carry out the Project in accordance with the Implementation Program set forth in Schedule 4 to this Agreement.

Section 3.02. Except as the Association 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 Credit shall be governed by the provisions of Schedule 3 to this Agreement.

Section 3.03. For the purposes of Section 9.06 of the General Conditions and without limitation thereto, the Borrower shall:

(a) prepare, on the basis of guidelines acceptable to the Association, and furnish to the Association 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 Association, a plan designed to ensure the continued achievement of the Project's objectives; and

(b) afford the Association a reasonable opportunity to exchange views with the Borrower on said plan.

ARTICLE IV

Financial Covenants

Section 4.01. (a) The Borrower shall maintain a financial management system, including records and accounts, and prepare financial statements in a format acceptable to the Association, adequate to reflect in accordance with sound financial management and accounting practices the operations, resources and expenditures related to the Project of the departments or agencies of the Borrower responsible for carrying out the Project or any part thereof.

(b) The Borrower shall:

(i) have the records, accounts and financial statements referred to in paragraph (a) of this Section including those for the Special Account for each Fiscal Year audited, in accordance with appropriate auditing principles consistently applied, by independent auditors acceptable to the Association;

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

(iii) furnish to the Association such other information concerning said records, accounts and financial statements, and the audit thereof, and concerning said auditors, as the Association may from time to time reasonably request.

(c) For all expenditures with respect to which withdrawals from the Credit Account were made on the basis of Project Management Reports or statements of expenditure, the Borrower shall:

(i) maintain or cause to be maintained, in accordance with paragraph (a) of this Section, records and separate accounts reflecting such expenditures;

(ii) retain or cause to be retained, until at least one year after the Association has received the audit report for the Fiscal Year in which the last withdrawal from the Credit Account was made, all records (contracts, orders, invoices, bills, receipts and other documents) evidencing such expenditures;

(iii) enable the Association's representatives to examine such records;
and

(iv) ensure that such records and accounts are included in the annual audit referred to in paragraph (b) of this Section and that the report of such audit contains a separate opinion by said auditors as to whether the Project Management Reports or statements of expenditure submitted during such Fiscal Year, together with the procedures and internal controls involved in their preparation, can be relied upon to support the related withdrawals.

Section 4.02. (a) Without limitation upon the provisions of Section 4.01 of this Agreement, the Borrower shall carry out a time-bound action plan acceptable to the Association for the strengthening of the financial management system referred to in paragraph (a) of said Section 4.01 in order to enable the Borrower, not later than February 28, 2001, or such later date as the Association shall agree, to prepare trimesterly Project Management Reports, acceptable to the Association, each of which:

(i) (A) sets forth actual sources and applications of funds for the Project, both cumulatively and for the period covered by said report, and projected sources and applications of funds for the Project for the eight-month period following the period covered by said report, and (B) shows separately expenditures financed out of the proceeds of the Credit during the period covered by said report and expenditures proposed to be financed out of the proceeds of the Credit during the eight-month period following the period covered by said report;

(ii) (A) describes physical progress in Project implementation, both cumulatively and for the period covered by said report, and (B) explains variances between the actual and previously forecast implementation targets; and

(iii) sets forth the status of procurement under the Project and expenditures under contracts financed out of the proceeds of the Credit, as at the end of the period covered by said report.

(b) Upon the completion of the action plan referred to in paragraph (a) of this Section, the Borrower shall prepare, in accordance with guidelines acceptable to the Association, and furnish to the Association not later than 45 days after the end of each trimester a Project Management Report for such period.

ARTICLE V

Remedies of the Association

Section 5.01. Pursuant to Section 6.02(1) of the General Conditions, the following additional event is specified, namely, that an event shall have occurred which shall make it improbable that the Priority Investment Plan or a significant part thereof will be carried out.

ARTICLE VI

Effective Date; Termination

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

(a) all bids have been received for contracts for all civil works for the first year of Project implementation and all proposals have been received for all consultants' services for institutional strengthening and training assistance;

(b) a Program Coordinator (Deputy Director General, Foreign Cooperation Branch of DOR), two Senior Divisional Engineers (including one Procurement Engineer), an Accounts Officer, an Accountant, an Environmental Engineer and a Social Planner have been appointed in the PCU;

(c) a draft of the proposed Nepal Roads Board Act or another equivalent legislation for the establishment of the Roads Board and the establishment of the Road Fund has been submitted to the Parliament Secretariat for the purpose of obtaining approval by the Parliament of the Borrower; and

(d) all actions set forth in the action plan referred to in Section 4.02(a) of this Agreement for which the completion dates specified therein precede the Effective Date have been completed.

Section 6.02. The date ninety (90) days after the date of this Agreement 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 Secretary, Ministry of Finance of the Borrower is designated as representative of the Borrower for the purposes of Section 11.03 of the General Conditions.

Section 7.02. The following addresses are specified for the purposes of Section 11.01 of the General Conditions:

For the Borrower:

Ministry of Finance
His Majesty's Government of Nepal
Kathmandu, Nepal

Cable address:

ARTHA
Kathmandu, Nepal

Telex:

2249-NEP

For the Association:

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

Cable address:

INDEVAS
Washington, D.C.

Telex:

248423 (MCI) or
64145 (MCI)

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

KINGDOM OF NEPAL

By /s/ Ram Binod Bhattarai

Authorized Representative

INTERNATIONAL DEVELOPMENT ASSOCIATION

By /s/ Hans M. Rothenbuhler

Country Director, Nepal

SCHEDULE 1

Withdrawal of the Proceeds of the Credit

A. General

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

Category	Amount of the Credit Allocated (Expressed in SDR Equivalent)	% of Expenditures to be Financed
(1) Civil works	27,800,000	100% of foreign expenditures and 55% of local expenditures
(2) Goods	700,000	100% of foreign expenditures, 100% of local expenditures (ex-factory cost) and 90% of local expend- itures for other items procured locally
(3) Consultants' services and training	7,300,000	100%
(4) Refunding of Project Preparation Advance	1,200,000	Amount due pursuant to Section 2.02(b) of this Agreement
(5) Unallocated	3,100,000	
TOTAL	<u>40,100,000</u> =====	

2. For the purposes of this Schedule:

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

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

3. Notwithstanding the provisions of paragraph 1 above, no withdrawals shall be made in respect of payments made for expenditures prior to the date of this Agreement, except that withdrawals, in an aggregate amount not exceeding the equivalent of SDR 3,700,000, may be made in respect of Categories (1), (2) and (3) set forth in the table in Part A.1 of this Schedule on account of payments made for expenditures before that date but after August 1, 1999.

4. The Association may require withdrawals from the Credit Account to be made on the basis of statements of expenditure for expenditures for: (a) goods under contracts costing less than \$50,000 equivalent each; (b) works under contracts costing less than \$200,000 equivalent each; (c) services under contracts costing less than \$50,000 equivalent each for employment of consulting firms and \$10,000 equivalent each for

employment of individual consultants; and (d) training; all under such terms and conditions as the Association shall specify by notice to the Borrower.

B. Special Account

1. The Borrower shall open and maintain in dollars a special deposit account in Nepal Rastra Bank, on terms and conditions satisfactory to the Association.

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

(a) until the Association shall have received (i) the first Project Management Report referred to in Section 4.02(b) of this Agreement and (ii) a request from the Borrower for withdrawal on the basis of Project Management Reports, withdrawals shall be made in accordance with the provisions of Annex A to this Schedule 1; and

(b) upon receipt by the Association of a Project Management Report pursuant to Section 4.02(b) of this Agreement, accompanied by a request from the Borrower for withdrawal on the basis of Project Management Reports, all further withdrawals shall be made in accordance with the provisions of Annex B to this Schedule 1.

3. Payments out of the Special Account shall be made exclusively for Eligible Expenditures. For each payment made by the Borrower out of the Special Account, the Borrower shall, at such time as the Association shall reasonably request, furnish to the Association 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 Association shall not be required to make further deposits into the Special Account:

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

(b) if the Association determines at any time that all further withdrawals should be made by the Borrower directly from the Credit Account; or

(c) if the Borrower shall have failed to furnish to the Association 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 Association pursuant to said Section in respect of the audit of (A) the records and accounts for the Special Account or (B) the records, accounts and financial statements reflecting expenditures with respect to which withdrawals were made on the basis of Project Management Reports or statements of expenditure.

5. The Association 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 Association shall have notified the Borrower of its intention to suspend in whole or in part the right of the Borrower to make withdrawals from the Credit Account pursuant to Section 6.02 of the General Conditions. Upon such notification, the Association shall determine, in its sole discretion, whether further deposits into the Special Account may be made and what procedures should be followed for making such deposits, and shall notify the Borrower of its determination.

6. (a) If the Association 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 Association, the Borrower shall, promptly upon notice from the Association, provide such additional evidence as the Association may request, or deposit into the Special Account (or, if the Association shall so request, refund to the Association) an amount equal to the amount of such payment. Unless the Association shall otherwise agree, no further deposit by the Association 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 Association determines at any time that any amount outstanding in

the Special Account will not be required to cover payments for Eligible Expenditures during the eight-month period following such determination, the Borrower shall, promptly upon notice from the Association, refund to the Association such outstanding amount.

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

(d) Refunds to the Association made pursuant to sub-paragraph (a), (b) or (c) of this paragraph 6 shall be credited to the Credit Account for subsequent withdrawal or for cancellation in accordance with the provisions of this Agreement.

Annex A to SCHEDULE 1

Operation of Special Account When Withdrawals Are Not Made On the Basis of Project Management Reports

1. For the purposes of this Annex, the term "Authorized Allocation" means an amount equivalent to \$2,000,000 to be withdrawn from the Credit Account and deposited into the Special Account pursuant to paragraph 2 of this Annex; provided, however, that unless the Association shall otherwise agree, the Authorized Allocation shall be limited to an amount equivalent to \$1,000,000 until the aggregate amount of withdrawals from the Credit Account, plus the total amount of all outstanding special commitments entered into by the Association pursuant to Section 5.02 of the General Conditions, shall equal or exceed the equivalent of SDR 1,500,000.

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 Association 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 Association shall, on behalf of the Borrower, withdraw from the Credit 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 Association requests for deposit into the Special Account at such intervals as the Association shall specify. Prior to or at the time of each such request, the Borrower shall furnish to the Association 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 Association shall, on behalf of the Borrower, withdraw from the Credit 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 Association from the Credit Account under one or more of the Eligible Categories.

3. The Association shall not be required to make further deposits into the Special Account, once the total unwithdrawn amount of the Credit, minus the total amount of all outstanding special commitments entered into by the Association 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 Credit Account of the remaining unwithdrawn amount of the Credit shall follow such procedures as the Association shall specify by notice to the Borrower. Such further withdrawals shall be made only after and to the extent that the Association shall have been satisfied that all such amounts remaining on deposit in the Special Account as of the date of such notice will be utilized in making payments for Eligible Expenditures.

Annex B to SCHEDULE 1

Operation of Special Account When Withdrawals Are Made On the Basis of Project Management Reports

1. Except as the Association may otherwise specify by notice to the Borrower, all withdrawals from the Credit Account shall be deposited by the Association 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 Association from the Credit Account under one or more of the Eligible Categories.

2. Each application for withdrawal from the Credit Account for deposit into the Special Account shall be supported by a Project Management Report.

3. Upon receipt of each application for withdrawal of an amount of the Credit, the Association shall, on behalf of the Borrower, withdraw from the Credit 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 Association has determined, based on the Project Management Report accompanying said application, is required to be deposited in order to finance Eligible Expenditures during the eight-month period following the date of such report; provided, however, that the amount so deposited, when added to the amount indicated by said Project Management Report to be remaining in the Special Account, shall not exceed the equivalent of \$8,000,000.

SCHEDULE 2

Description of the Project

The objectives of the Project are to assist the Borrower in: (i) strengthening the road sector planning by building upon the Priority Investment Plan framework; (ii) reducing vehicle transport costs and delays; (iii) improving the access to district headquarters not currently served by road; (iv) promoting more sustainable funding and more efficient public sector management of road maintenance; and (v) generating temporary rural employment through adoption of labor-based road construction technologies and long-term employment for road maintenance and additional economic activities generated by the improved road network.

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

Part A: Policy Reform

Implementing policy reform in the road sector to achieve sustainable maintenance management of the strategic, urban and rural road network through, inter alia: (i) the establishment and implementation of the Roads Board with public and private sector participation to oversee the management of the maintenance of such network and financial allocations for maintenance in the road sector; and (ii) the establishment and operation of the Road Fund to increase funding for road maintenance through enhanced road user contributions and efficiency of expenditures.

Part B: Road Construction and Upgrading

1. Constructing about 200 km of new dry-weather feeder roads and upgrading about 260 km of existing dry-weather feeder roads to gravel road standard.
2. Carrying out a program of resettlement and rehabilitation of people affected by the carrying out of Part B.1 of the Project.

Part C: Road Rehabilitation

1. Rehabilitating about 160 km of the strategic highway and feeder road network.
2. Carrying out a program of resettlement and rehabilitation of people affected by the carrying out of Part C.1 of the Project.

Part D: Road Maintenance

Implementing periodic maintenance of about 470 km of the strategic highway and feeder road network.

Part E: Institutional Strengthening and Training

Strengthening the institutional capacity of MOWT/DOR through: (i) the provision

of support and training to (a) the Road Sector Skills Development Unit of DOR for local training, (b) the Geo-Environmental Unit of DOR to expand its capabilities in the implementation of environmental management action plans and resettlement and rehabilitation plans, (c) the Mechanical Training Center of DOR to assist with its commercialization, continuation of mechanical training and expansion of training to cover private sector personnel, (d) the Chief Technical Examiner Section of MOWT to enable it to establish a technical audit capacity and to undertake technical audits of DOR projects, and (e) the Planning and Design Branches of DOR for activities related to the existing Maintenance and Rehabilitation Coordination Unit of DOR and the Traffic Engineering and Safety Unit of DOR; (ii) the undertaking of semi-annual third-party operational audits of DOR's operations; (iii) the undertaking of pre-investment studies and socio-economic impact studies of Project beneficiaries; (iv) the provision of equipment for office modernization and vehicles for field surveys and inspections; and (v) improvements to training and office facilities.

* * *

The Project is expected to be completed by June 30, 2004.

SCHEDULE 3

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 provisions of the following Parts of this Section I.

Part B: International Competitive Bidding

1. Except as otherwise provided in Part C of this Section, goods and works shall be procured under contracts awarded in accordance with the provisions of Section II of the Guidelines and paragraph 5 of Appendix I thereto.

2. The following provisions shall apply to goods and works to be procured under contracts awarded in accordance with the provisions of paragraph 1 of this Part B.

(a) Prequalification

Bidders for contracts for works estimated to cost \$2,000,000 equivalent or more per contract shall be prequalified in accordance with the provisions of paragraphs 2.9 and 2.10 of the Guidelines.

(b) Grouping of Contracts

To the extent practicable, contracts for goods shall be grouped in bid packages estimated to cost \$200,000 equivalent or more each.

(c) Preference for domestically manufactured goods and domestic contractors

The provisions of paragraphs 2.54 and 2.55 of the Guidelines and Appendix 2 thereto shall apply to goods manufactured in the territory of the Borrower and works to be carried out by domestic contractors.

Part C: Other Procurement Procedures

1. National Competitive Bidding

(a) The following may be procured under contracts awarded in accordance with the provisions of paragraphs 3.3 and 3.4 of the Guidelines: (i) works estimated to cost less than \$500,000 equivalent per contract, up to an aggregate amount not to exceed \$22,000,000 equivalent; and (ii) goods estimated to cost less than \$200,000

equivalent per contract, up to an aggregate amount not to exceed \$300,000 equivalent.

(b) In order to ensure economy, efficiency, transparency and broad consistency with the provisions of Section 1 of the Guidelines:

- (i) invitations to bid shall be advertised in at least one widely circulated national daily newspaper, at least 30 days prior to the deadline for the submission of bids;
- (ii) bid documents shall be made available, by mail or in person, to all who are willing to pay the required fee;
- (iii) evaluation of bids shall be made in strict adherence to the criteria disclosed in the bidding documents, in a format and specified period agreed with the Association;
- (iv) bids shall be opened in public in one place, immediately after the deadline for submission of bids;
- (v) foreign bidders shall not be precluded from bidding and no preference of any kind shall be given to national bidders;
- (vi) qualification criteria (in case pre-qualifications were not carried out) shall be stated in the bidding documents, and if a registration process is required, a foreign firm declared as the lowest evaluated bidder shall be given a reasonable opportunity of registering, without let or hindrance;
- (vii) contracts shall be awarded to the lowest evaluated bidders;
- (viii) post-bidding negotiations shall not be allowed with the lowest evaluated bidders or any other bidders;
- (ix) bids shall not be rejected merely on the basis of a comparison with an official estimate without the prior concurrence of the Association;
- (x) contracts shall not be awarded on the basis of nationally negotiated rates;
- (xi) re-bidding shall not be carried out without the prior concurrence of the Association;
- (xii) all bidders/contractors shall provide bid/performance security as indicated in the bidding/contract documents;
- (xiii) a bidder's bid security shall apply only to a specific bid, and a contractor's performance security shall apply only to the specific contract under which it was furnished;
- (xiv) split award or lottery in award of contracts shall not be carried out. When two or more bidders quote the same lowest price, an investigation shall be made to determine any evidence of collusion, following which (A) if collusion is determined, the parties involved shall be disqualified and the award shall then be made to the next lowest evaluated and qualified bidder and (B) if no evidence of collusion can be confirmed, then fresh bids shall be invited after receiving the concurrence of the Association;
- (xv) extension of bid validity shall not be allowed without the prior concurrence of the Association (A) for the first request for extension if it is longer than eight weeks and (B) for all subsequent requests for extension irrespective of the period;
- (xvi) bids shall not be invited on the basis of percentage premium or discount over the estimated cost; and

(xvii) there shall not be any restrictions on the means of delivery of the bids.

2. International or National Shopping

Goods estimated to cost less than \$50,000 equivalent per contract, up to an aggregate amount not to exceed \$200,000 equivalent, may be procured under contracts awarded on the basis of shopping procedures in accordance with the provisions of paragraphs 3.5 and 3.6 of the Guidelines.

3. Procurement of Small Works

Works estimated to cost less than \$30,000 equivalent per contract, up to an aggregate amount not to exceed \$2,000,000 equivalent, may be procured under lump-sum, fixed-price contracts awarded on the basis of quotations obtained from at least 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 Association, 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

Works estimated to cost less than \$50,000 equivalent per contract, up to an aggregate amount not to exceed \$2,000,000 equivalent when added to the works procured under paragraph 5 of this Part C, may be procured by community participation in accordance with the provisions of paragraph 3.15 of the Guidelines and procedures acceptable to the Association.

5. Direct Contracting

The following may, with the Association's prior agreement, be procured by direct contracting in accordance with the provisions of paragraph 3.7 of the Guidelines: (a) works estimated to cost less than \$20,000 equivalent per contract, up to an aggregate amount not to exceed \$2,000,000 equivalent when added to the works procured under paragraph 4 of this Part C; and (b) computer software for the financial management system up to an aggregate amount not to exceed \$8,000 equivalent.

Part D: Review by the Association of Procurement Decisions

1. Procurement Planning

Prior to the issuance of any invitations to prequalify for bidding or to bid for contracts, the proposed procurement plan for the Project shall be furnished to the Association for its review and approval, in accordance with the provisions of paragraph 1 of Appendix 1 to the Guidelines. Procurement of all goods and works shall be undertaken in accordance with such procurement plan as shall have been approved by the Association, and with the provisions of said paragraph 1.

2. Prior Review

(a) With respect to (i) each contract for works estimated to cost the equivalent of \$200,000 or more and (ii) each contract for goods estimated to cost the equivalent of \$50,000 or more, the procedures set forth in paragraphs 2 and 3 of Appendix 1 to the Guidelines shall apply.

(b) With respect to (i) each contract for goods to be procured under paragraph 2 of Part C above, (ii) the first three contracts for works to be procured under paragraph 3 of Part C above, (iii) each contract for works to be procured under paragraph 4 of Part C above and estimated to cost the equivalent of \$30,000 or more and (iv) each contract for goods and works to be procured under paragraph 5 of Part C above, the following procedures shall apply:

(i) prior to the selection of any supplier under shopping or three-quotation procedures, the Borrower shall provide to the Association a report on the comparison and evaluation of

quotations received;

(ii) prior to the execution of any contract referred to in this paragraph 2(b), the Borrower shall provide to the Association a copy of the specifications and the draft contract; and

(iii) the procedures set forth in paragraphs 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 and January 1999 (the Consultant Guidelines) and the provisions of the following Parts of this Section II.

Part B: Quality- and Cost-based Selection

1. Except as otherwise provided in Part C of this Section, consultants' services shall be procured under contracts awarded in accordance with the provisions of Section II of the Consultant Guidelines, paragraph 3 of Appendix 1 thereto, Appendix 2 thereto, and the provisions of paragraphs 3.13 through 3.18 thereof applicable to quality- and cost-based selection of consultants.

2. The following provisions shall apply to consultants' services to be procured under contracts awarded in accordance with the provisions of the preceding paragraph. The short list of consultants for services, estimated to cost less than \$200,000 equivalent per contract, may comprise entirely national consultants in accordance with the provisions of paragraph 2.7 of the Consultant Guidelines.

Part C: Other Procedures for the Selection of Consultants

1. Selection under a Fixed Budget

Services for assisting the Borrower in the implementation and monitoring of a program of resettlement and rehabilitation and environmental management under Parts B and C of the Project may be procured under contracts awarded in accordance with the provisions of paragraphs 3.1 and 3.5 of the Consultant Guidelines.

2. Individual Consultants

Services for tasks that meet the requirements set forth in paragraph 5.1 of the Consultant Guidelines shall be procured under contracts awarded to individual consultants in accordance with the provisions of paragraphs 5.1 through 5.3 of the Consultant Guidelines.

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

1. Selection Planning

Prior to the issuance to consultants of any requests for proposals, the proposed plan for the selection of consultants under the Project shall be furnished to the Association for its review and approval, in accordance with the provisions of paragraph 1 of Appendix 1 to the Consultant Guidelines. Selection of all consultants' services shall be undertaken in accordance with such selection plan as shall have been approved by the Association, and with the provisions of said paragraph 1.

2. Prior Review

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

(b) With respect to each contract for the employment of consulting firms estimated to cost the equivalent of \$50,000 or more, but less than the equivalent of \$100,000, the procedures set forth in paragraphs 1, 2 (other than the second subparagraph of paragraph 2(a)) and 5 of Appendix 1 to the Consultant Guidelines shall apply.

(c) With respect to each contract for the employment of individual consultants estimated to cost the equivalent of \$10,000 or more, the qualifications, experience, terms of reference and terms of employment of the consultants shall be furnished to the Association for its prior review and approval. The contract shall be awarded only after the said approval shall have been given.

(d) With respect to each proposal for overseas training or overseas study tour, cost estimates and a description of the type and purpose of such training or study tour shall be furnished to the Association for its prior review and approval. The training or study tour, as applicable, shall be undertaken only after the said approval shall have been given.

3. Post Review

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

SCHEDULE 4

Implementation Program

Project Implementation Plan

1. The Borrower shall carry out the Project in accordance with the Project Implementation Plan.

Project Coordination and Implementation Unit (PCU)

2. The Borrower shall maintain the PCU with adequate numbers of professional staff with skills and experience and on terms of reference satisfactory to the Association, including without limitation (i) a Program Coordinator (Deputy Director General, Foreign Cooperation Branch), (ii) two Senior Divisional Engineers (including one Procurement Engineer), (iii) an Accounts Officer, (iv) two Accountants, (v) an Environmental Engineer, (vi) a Social Planner and (vii) two Assistant Engineers.

3. The Borrower shall ensure that the key staff in the PCU listed in the preceding paragraph will not be transferred to other positions during the period of Project implementation (and in the case of the Accounts Officer, for the additional six months following the Closing Date), except with prior notice to the Association and as required by the applicable law of the Borrower.

Geo-Environmental Unit

4. The Borrower shall: (i) by December 31, 2000, submit to the Association a specific action plan, satisfactory to the Association, for strengthening the capabilities of the Geo-Environmental Unit of DOR, including without limitation its capacity for preparing and monitoring environmental and social impact assessments; and (ii) thereafter implement such action plan in a manner satisfactory to the Association and submit to the Association on a quarterly basis a report of all the activities undertaken by such Unit.

Beneficiary Impact Assessment

5. By October 31, 2001 and May 31, 2003, the Borrower shall: (i) conduct in a manner and with terms of reference satisfactory to the Association a socio-economic

assessment of impacts on Project beneficiaries of the road improvements made under the Project during the period preceding each such date, with the beneficiary participation in data collection and impact monitoring; and (ii) submit a report of each such assessment to the Association. Financial Management System

6. The Borrower shall: (i) by February 29, 2000, complete the preparation of an accounts manual, satisfactory to the Association, for the operation of its financial management system; (ii) by March 31, 2000, start the training, with terms of reference satisfactory to the Association, of the adequate number of accounts staff of the PCU by using such accounts manual; and (iii) by February 29, 2000, appoint an assistant to the Procurement Engineer and a computer technician for the operation of the financial management system, both with qualifications and experience satisfactory to the Association.

Roads Board and Road Fund

7. By December 31, 2001, the Borrower shall make the Roads Board and the Road Fund operational under the Nepal Roads Board Act or another equivalent legislation referred to in Section 6.01(c) of this Agreement, including the issuance of all necessary or appropriate regulations under such Act or equivalent legislation, in a manner satisfactory to the Association.

Survey of Quality of Road Works

8. As part of the third-party operational audits of DOR's operations under Part E of the Project, the Borrower shall: (i) by June 30 and December 31 of each year, arrange for a sample survey, with the scope and content satisfactory to the Association, of the overall quality of road construction and maintenance works carried out by DOR, to be conducted by an independent monitoring engineer with qualifications, experience and terms of reference satisfactory to the Association, and submit the results of each such survey to the Association; and (ii) thereafter implement in a manner satisfactory to the Association the recommendations resulting from each such survey.

Survey of Road Roughness and Visual Condition Rating

9. By May 31 of each year, the Borrower shall: (i) conduct a survey of road roughness and visual condition rating on at least 50% of strategic highways and feeder roads of the Borrower (focusing on the strategic highway network and incrementally covering the rest of the network); and (ii) disseminate the results of each such survey in the Road Condition Report published by the Borrower.

Road Maintenance Funding

10. During the period of Project implementation, the Borrower shall ensure that the annual allocations and expenditures for the maintenance of roads (comprising the strategic road network of highways and feeder roads managed by DOR), consisting of routine, periodic, recurrent and emergency maintenance expenditures but excluding funds contributed by external donors and other agencies and funds allocated to construction and upgrading works, will be systematically increased for each Fiscal Year to not less than the following amounts: NRs 700 million in FY1999/2000; NRs 850 million in FY2000/01; NRs 950 million in FY2001/02; NRs 1,050 million in FY2002/03; and NRs 1,150 million in FY2003/04.

Road Maintenance Planning, Programming and Implementation

11. The Borrower shall: (i) by March 1, 2000, submit to the Association an action plan, satisfactory to the Association, for strengthening DOR's capabilities for road maintenance planning, programming and implementation; and (ii) thereafter implement such action plan in a manner satisfactory to the Association, including without limitation the implementation of the exit strategy for the Maintenance and Rehabilitation Coordination Unit of DOR and the streamlining of the maintenance planning and programming activities in the Planning Branch of DOR, by the earlier of (a) September 1, 2000 or (b) the award of the contracts for maintenance works for the second year of Project implementation.

Roads Not Included in Project Implementation Plan

12. The Borrower shall not use any part of the proceeds of the Credit to undertake civil works on any roads not included in the Project Implementation Plan, unless and until the Borrower has submitted to the Association documentation satisfactory to the Association for undertaking civil works for such roads, including without limitation a feasibility study report, an environmental management plan and a resettlement action plan.

Labor-based Road Construction Technologies

13. The Borrower shall ensure that labor-based road construction technologies and local contractors and road user groups will be employed in the carrying out of the new road construction works under Part B.1 of the Project to the maximum extent possible and in a manner satisfactory to the Association.

Environmental Management Action Plans

14. The Borrower shall implement the mitigation, monitoring and evaluation and all other actions set forth in the EIA, the IEEs and the EMAPs in accordance with the objectives, policies, procedures, time schedules and other provisions set forth therein and shall not take any action which would prevent or interfere with such implementation. Environmental Mitigation Measures in Civil Works Contracts

15. The Borrower shall ensure that all civil works contracts, bid documents and bills of quantities for the roads covered by the Project will include the environmental mitigation measures set forth in the EIA, the IEEs, the EMAPs and the Environmental Management Guidelines of the Borrower published by DOR.

Resettlement Action Plan

16. The Borrower shall:

(a) implement the RAP in accordance with the objectives, policies, procedures, time schedules and other provisions set forth therein and shall not take any action which would prevent or interfere with such implementation;

(b) submit to the Association updates to the RAP, satisfactory to the Association, based on detailed socio-economic surveys of project affected people and consistent with the principles set forth in the RAP, for those roads included in Part B.1 or C.1 of the Project for which such surveys had not been completed or engineering designs had not been finalized as of July 1999, before bids relating to works for such roads are invited or, if no bidding process is involved, before a contractor for works for such roads is selected in accordance with the provisions of Schedule 3 to this Agreement; and

(c) implement the RAP with the updates referred to in subparagraph (b) of this paragraph in accordance with the objectives, policies, procedures, time schedules and other provisions set forth therein and shall not take any action which would prevent or interfere with such implementation.

Trimesterly Reports

17. The Borrower shall, within forty-five (45) days after the end of each trimester, provide to the Association a trimesterly report setting forth (i) the progress of the Project implementation and the achievement of the indicators referred to in paragraph 18 below and (ii) proposed action plans for each Part of the Project for the following trimester.

Monitoring and Evaluation; Mid-Term Review

18. The Borrower shall:

(a) maintain policies and procedures adequate to enable it to monitor and evaluate on an ongoing basis, in accordance with indicators satisfactory to the Association, the carrying out of the Project and the achievement of the objectives thereof;

(b) prepare, under terms of reference satisfactory to the Association, and furnish to the Association, by October 31, 2001, a report integrating the results of the monitoring and evaluation activities performed pursuant to subparagraph (a) of this paragraph, on the progress achieved in the carrying out of the Project during the period preceding the date of said report and setting out the measures recommended to ensure the efficient carrying out of the Project and the achievement of the objectives thereof during the period following such date; and

(c) review with the Association, by November 30, 2001, or such later date as the Association shall request, the report referred to in subparagraph (b) of this paragraph and, thereafter, 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 report and the Association's views on the matter.

