

CONFORMED COPY

CREDIT NUMBER 3247-MOZ

Development Credit Agreement

(Second National Water Development Project)

between

REPUBLIC OF MOZAMBIQUE

and

INTERNATIONAL DEVELOPMENT ASSOCIATION

Dated October 6, 1999

CREDIT NUMBER 3247-MOZ

DEVELOPMENT CREDIT AGREEMENT

AGREEMENT, dated October 6, 1999, between REPUBLIC OF MOZAMBIQUE (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, has requested the Association to assist in the financing of the Project;

(B) the Association has received a letter, dated September 16, 1997, from the Borrower describing a program of actions, objectives and policies designed to strengthen the Borrower's water sector (the Program) and declaring the Borrower's commitment to the execution of the Program;

(C) Parts A and B of the Project will be carried out by Fundo de Investimento e Patrimônio do Abastecimento de Água (FIPAG) with the Borrower's assistance and, as part of such assistance, the Borrower will make available to FIPAG part of the proceeds of the Credit as provided in this Agreement;

(D) the Borrower intends to contract from the African Development Bank (African Development Bank (AfDB)) a loan (the AfDB Loan)

in an amount equivalent to \$19,600,000 to assist in financing the Project on the terms and conditions set forth in an agreement (the AfDB Loan Agreement) to be entered into between the Borrower and AfDB; and

(E) the Borrower intends to contract from Kingdom of the Netherlands (Netherlands) a grant (the Dutch Grant) in an amount equivalent to \$10,000,000 to assist in financing the Project on the terms and conditions set forth in an agreement (the Dutch Grant Agreement) to be entered into between the Borrower and Netherlands; and

WHEREAS the Association has agreed on the basis, inter alia, of the foregoing, to extend the Credit to the Borrower upon the terms and conditions set forth in this Agreement and in the Project Agreement of even date herewith between the Association and FIPAG;

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), with the modifications set forth below (the General Conditions) constitute an integral part of this Agreement:

(a) A new paragraph 12 is added to Section 2.01 to read as set forth below, and the existing paragraphs 12 through 14 of said Section are accordingly renumbered as paragraphs 13 through 15:

"12. 'Participating Country' means any country that the Association determines meets the requirements set forth in Section 10 of Resolution No. 183 of the Board of Governors of the Association, adopted on June 26, 1996; and 'Participating Countries' means, collectively, all such countries."

(b) The second sentence of Section 5.01 is modified to read:

"Except as the Borrower and the Association shall otherwise agree, no withdrawals shall be made: (a) on account of expenditures in the territories of any country which is not a Participating Country or for goods produced in, or services supplied from, such territories; or (b) for the purpose of any payment to persons or entities, or for any import of goods, if such payment or import, to the knowledge of the Association, is prohibited by a decision of the United Nations Security Council taken under Chapter VII of the Charter of the United Nations."

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) "CRA" means Conselho de Regulaçao do Abastecimento de Agua, the Borrower's Council for Regulation of Water Supply;

(b) "DNA" means the Direçcao Nacional de Aguas, the National Directorate of Water within MOPH (as hereinafter defined);

(c) "Delegated works and goods" means the works and goods procured in accordance with the provisions of Part C.5 of Section II of Schedule 3 to this Agreement, and required for: (i) initial rehabilitation of main and connections, (ii) provision of new connections and meter, and (iii) vehicles, plant and equipment for construction and operation, all of which were contained in the competitive bid obtained for award of the contract to the Private Operator (as hereinafter defined);

(d) "Environmental Management Plan" means the environmental management plan adopted by the Borrower on April 9, 1999;

(e) "Lease contract" means the contract entered into between FIPAG and the Private Operator (as hereinafter defined) for the operation of urban water supply systems in the city of Maputo, as the same may be amended from time to time, and such term includes all schedules and agreements supplemental to said contract;

(f) "Management Contracts" means any of the contracts entered into between FIPAG and the Private Operator for the operation of water supply systems in the cities of Beira, Nampula, Pemba and Quelimane (collectively referred to as the four cities), as the same may be amended from time to time, and such term includes all schedules and agreements supplemental to said contract;

(g) "Mozambican Metical" and "MT" mean the currency of the Borrower;

(h) "MOPH" means Ministerio das Obras Publicas e Habitacao, the Borrower's Ministry of Public Works and Housing;

(i) "Performance Indicators" means indicators referred to in Schedule 6 to this Agreement;

(j) "Contrato-programa" means the contract to be entered into between the Borrower and FIPAG, pursuant to Section 6.01 (d) of this Agreement, and in accordance with the Borrower's decree 73/98, dated December 23, 1998, providing for FIPAG's performance targets and obligations for reporting, as the same may be amended from time to time, and such term includes all schedules and agreements supplemental to said agreement;

(k) "Private Operator or PO " means a company incorporated under the laws of the Borrower, and which shall enter into a lease or management contract (as the case may be) with FIPAG to carry out the technical and commercial operation of water supply services in the city of Maputo and the four cities;

(l) "Project Account" means the account referred to in Section 3.07 (a) of this Agreement;

(m) "Project Agreement" means the agreement between the Association and FIPAG of even date herewith, as the same may be amended from time to time, and such term includes all schedules and agreements supplemental to the Project Agreement;

(n) "Project Implementation Manual" means the manual adopted by the Borrower pursuant to Section 6.01 (g) of this Agreement containing, inter alia, work plans, training plans and procedures to be used for the purpose of implementation of the Project, and such term includes any schedules to the Project Implementation Manual;

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

(p) "Special Account" means the account referred to in Section 2.02 (b) of this Agreement; and

(q) "Subsidiary Loan Agreement" means the agreement to be entered into between the Borrower and FIPAG pursuant to Section 3.03 (a) of this Agreement, as the same may be amended from time to time, and such term includes all schedules to the Subsidiary Loan 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 the Development Credit Agreement, an amount in various currencies equivalent to fifty five million four hundred thousand Special Drawing Rights (SDR 55,400,000).

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 described in Schedule 2 to this Agreement and to be financed out of the proceeds of the Credit.

(b) The Borrower may, for the purposes of the Project, open and maintain in Dollars, in the name of FIPAG, a separate special deposit account (the Special Account) in a commercial bank on terms and conditions satisfactory to the Association, including appropriate protection against set-off, seizure and attachment. 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 September 30, 2005, 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 1 and September 1 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 semi-annual installments payable on each March 1 and September 1 commencing September 1, 2009 and ending March 1, 2039. Each installment to and including the installment payable on March 1, 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. The Borrower declares its commitment to the objectives of the Project as set forth in Schedule 2 to this Agreement, and, to this end:

(a) shall carry out Part C of the Project with due diligence and efficiency and in conformity with appropriate administrative, financial, engineering, and environmental practices, and shall provide, promptly as needed, the funds, facilities, services and other resources required for Part C of the Project; and

(b) without any limitation or restriction upon any of its other obligations under the Development Credit Agreement, shall cause FIPAG to perform in accordance with the provisions of the FIPAG Project Agreement all the obligations of FIPAG therein set forth, shall take and cause to be taken all action, including the provision of funds, facilities, services and other resources, necessary or appropriate to enable FIPAG to perform such obligations, and shall not take or permit to be taken any action which would prevent or interfere with such performance.

Section 3.02. 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 Part C of the Project and cause FIPAG to carry out Parts A and B of the Project, all in accordance with the Implementation Program set forth in Schedule 4 to this Agreement.

Section 3.03. (a) For the purposes of Parts A and B of the Project, the Borrower shall relend the proceeds of the Credit allocated from time to time to Category (1) of the table in paragraph 1 of Schedule 1 to this Agreement to FIPAG under a subsidiary loan agreement to be entered into between the Borrower and FIPAG (the Subsidiary Loan Agreement) under terms and conditions which shall have been approved by the Association, and which shall include that the proceeds of the Credit be onlent with a repayment period of 22 years including a grace period of 5 years and an interest rate of 6.25% per annum.

(b) The Borrower shall exercise its rights under the Subsidiary Loan Agreement in such manner as to protect the interests of the Borrower and the Association and to accomplish the purposes of the Credit, and, except as the Association shall otherwise agree, the Borrower shall not assign, amend, abrogate or waive the Subsidiary Loan Agreement or any provision thereof.

Section 3.04. 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 3.05. For the purposes of Section 9.07 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 for the future operation of Part C of the Project; and

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

Section 3.06. The Borrower and the Association hereby agree that the obligations set forth in Sections 9.03, 9.04, 9.05, 9.06, 9.07 and 9.08 of the General Conditions (relating to insurance, use of goods and services, plans and schedules, records and reports, maintenance and land acquisition, respectively) in respect of Parts "A" and "B" of the Project shall be carried out by FIPAG pursuant to Section 2.03 of the Project Agreement.

Section 3.07. Without limitation to its obligations under Section 3.01 of this Agreement, the Borrower shall:

(a) open and maintain, in the name of FIPAG, an account (the Project Account) in MT in a commercial bank on terms and conditions satisfactory to the Association;

(b) not later than December 31, 1999, make an initial deposit into such account, in an amount equivalent to \$250,000, to finance the Borrower's contribution to the Project;

(c) thereafter, deposit into the Project Account by March 31, June 30, September 30 and December 31, in each year, an amount equivalent to \$175,000, until an amount equivalent to \$2,000,000 is reached; and

(d) use the Project Account funds exclusively to finance expenditures under the Project.

Section 3.08. The Borrower shall:

(a) ensure that the tariffs charged on water will reflect the principles of full cost recovery and be sufficient to cover operating expenses, depreciation and cost of capital, and tariff levels shall be assessed during the mid-term review referred to in paragraph 5(c) of Schedule 4 to this Agreement;

(b) take all measures necessary to ensure that all the Borrower's agencies pay their invoices for water supply services within the terms of trade;

(c) no later than 12 months after the Effective Date, settle all its outstanding arrears to the utilities covered under the Project;

(d) no later than March 31, 2000, appoint the members of the Board and the Chairman of CRA; and

(e) cause CRA to: (i) no later than June 30, 2000, prepare and furnish to the Association, a staffing plan and benefits package for CRA; and (ii) no later than December 31, 2000, appoint all the necessary staff.

ARTICLE IV

Financial Covenants

Section 4.01. (a) The Borrower shall maintain or cause to be maintained records and accounts adequate to reflect in accordance with sound accounting practices the operations, resources and expenditures in respect of Part C of 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 and accounts 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 four months after the end of each such year, the 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 and accounts and the audit thereof as the Association shall 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 statements of expenditure, the Borrower shall:

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

(ii) retain, 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 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 its financial management system for the Project in order to enable the Borrower, not later than eighteen months after the Effective Date, or such later date as the Association shall agree, to prepare quarterly 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 six-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 six-month period following the period covered by said report;

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

(iii) sets forth the status of procurement under the Project and expenditures under contracts financed out of the proceeds of the 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 calendar quarter 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 events are specified:

(a) A situation shall have arisen which shall make it improbable that the Program or a significant part thereof will be carried out.

(b) FIPAG shall have failed to perform any of its obligations under the Project Agreement.

(c) As a result of events which have occurred after the date of the Development Credit Agreement, an extraordinary situation shall have arisen which shall make it improbable that FIPAG will be able to perform its obligations under the Project Agreement.

(d) (i) Subject to subparagraph (ii) of this paragraph:

(A) the right of the Borrower to withdraw the proceeds of the AfDB Loan or the Dutch Grant made to the Borrower for the financing of the Project shall have been suspended, canceled or terminated in whole or in part, pursuant to the terms of the agreement providing therefor, or

(B) the AfDB loan shall have become due and payable prior to the agreed maturity thereof.

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

(A) such suspension, cancellation, termination or prematuring is not caused by the failure of the Borrower to perform any of its obligations under such agreement; and

(B) adequate funds for the Project are available to the Borrower from other sources on terms and conditions consistent with the obligations of the Borrower under this Agreement;

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

(a) the events specified in paragraphs (b), (c) of Section 5.01 of this Agreement shall occur and shall continue for a period of 30 days after notice thereof shall have been given by the Association to the Borrower; and

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

ARTICLE VI

Effective Date; Termination

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

(a) the AfDB Loan Agreement has been executed and delivered and all conditions precedent to its effectiveness or to the right of the Borrower to make withdrawals thereunder, except only the effectiveness of the Credit Agreement, have been fulfilled;

(b) the Dutch Grant Agreement has been executed and delivered and all conditions precedent to its effectiveness or to the right of the Borrower to make withdrawals thereunder, except only the effectiveness of the Credit Agreement, have been fulfilled;

(c) the chief executive officer, with terms of reference and qualifications acceptable to the Association, has been appointed;

(d) the Contrato-programa, in form and substance acceptable to the Association, has been entered into;

(e) FIPAG has entered into the Lease Contract and the Management Contract with the winning bidder for the management of city water supply systems of Maputo, Beira, Quelimane, Nampula, and Pemba;

(f) DNA and FIPAG have established accounting services, acceptable to the Association;

(g) the Borrower has adopted the Project Implementation Manual, in form and substance acceptable to the Association; and

(h) the Subsidiary Loan Agreement has been executed on behalf of the Borrower and FIPAG.

Section 6.02. The following are specified as additional matters,

within the meaning of Section 12.02 (b) of the General Conditions, to be included in the opinion or opinions to be furnished to the Association:

(a) that the Project Agreement has been duly authorized or ratified by FIPAG, and is legally binding upon FIPAG in accordance with its terms; and

(b) that the Subsidiary Loan Agreement has been duly authorized or ratified by the Borrower and FIPAG and is legally binding upon the Borrower and FIPAG in accordance with its terms.

Section 6.03. 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 Governor of the Central Bank 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:

Banco de Mocambique
Departamento de Relacoes Internacionais
Avenida 25 de Setembro
P.O. Box 423

Cable address:

MOBANCO
Maputo

Telex:

6355/BMMO

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 the District of Columbia, United States of America, as of the day and year first above written.

REPUBLIC OF MOZAMBIQUE

By /s/ Marcos Namashulua
Authorized Representative

INTERNATIONAL DEVELOPMENT ASSOCIATION

By /s/ Callisto Madavo

Regional Vice President
Africa

SCHEDULE 1

Withdrawal of the Proceeds of the Credit

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:

% of	Amount of the Credit	
Expenditures	Allocated (Expressed	
Category	in SDR Equivalent)	to be
Financed		
(1) Civil works foreign	14,990,000	100% of
expenditures and		
local		90% of
expenditures		
(2) Consultants' services, including audit		100%
(a) For Parts A and B	24,140,000	
(b) For Part C	3,100,000	
(3) Goods foreign		100% of
expenditures and		
local		90% of
expenditures		
(a) For Parts A and B (including vehicles)	1,780,000	
(b) Vehicles under Part C	230,000	
(4) Training	590,000	100%
(5) Operating Costs local	2,510,000	100% of
expenditures until		
December 31, 2002,		
of local		and 70%

expenditures,

thereafter

(6)	Unallocated	8,060,000
	TOTAL	<u>55,400,000</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;

(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; and

(c) the term "Operating Costs" means incremental local expenditures incurred on account of Project implementation, including office consumables (including communication expenses), utility costs, staff travel and associated subsistence allowances, office rental, office supplies and maintenance, and fuel and maintenance for vehicles and equipment, but excluding salaries of the Borrower's civil servants.

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.

4. The Association may require withdrawals from the Credit Account to be made on the basis of statements of expenditure for expenditures for:
(i) works under contracts costing less than \$250,000 equivalent each;
(ii) goods under contracts costing less than \$200,000 equivalent each;
(iii) services of consulting firms under contracts costing less than \$100,000 equivalent each; (iv) services of individual consultants under contracts costing less than \$50,000 equivalent each; and (v) training and operating costs, under such terms and conditions as the Association shall specify by notice to the Borrower.

SCHEDULE 2

Description of the Project

The objectives of the Project are to: (i) improve the quality, reliability, coverage and sustainability of water services for the cities of Maputo, Beira, Quelimane, Nampula, and Pemba through the promotion of greater private sector participation in the provision of these services; (ii) commence institutional and regulatory reform within the urban water sector with the introduction of commercial principles in the operation and management of water services through the use of a private sector operator; (iii) accelerate capacity building and human resource development for the sector through training and demonstration effects within the context of the private operator contract; and (iv) provide an institutional framework that improves the quality and sustainability of users services and acts as an operational model for water services in other cities.

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: Private Sector Management of Water Supply

1. Carrying out, through a 15-year lease contract, of the operation of the water supply system of Maputo including rehabilitation of water

supply network, installation of new connections, replacement of mains and meters.

2. Carrying out, through five-year contracts for management services, of operation and maintenance of the water supply systems in Beira, Quelimane, Nampula and Pemba, including management of staff, recurrent funds, meter reading, and collections.

3. Provision of technical advisory services and logistical assistance for the management by the Private Operator, of the activities referred to in (1) and (2) of this Part, including surveys, plans, and studies.

4. Provision of technical advisory services and logistical assistance for the procurement of design consultancies, construction contracts, supervision of design and construction, and commissioning of works.

5. Provision of vehicles, mobile plant, office equipment and computers for water supply operations in Beira, Quelimane, Nampula and Pemba.

6. Provision of computers, office equipment and furniture, vehicles, and water supply instrumentation to FIPAG.

7. Provision of technical advisory services and logistical assistance to FIPAG in project management, financial management, accounting, construction management and environment management.

8. Carrying out of a human resources development and training program for water supply employees (excluding on-the-job training, and excluding the PO's own staff), and staff of FIPAG.

Part B: Water Supply Works

1. Carrying out of water supply works for the city of Maputo and the four cities, including, water treatment work (WTW), transmission pipelines, new filters, equipment replacement, construction and repairs of tanks, metering works, upgrading of pumping stations, expansion or development of water and sanitation systems, booster pumping station, refurbishment, development of new water source, wellfield and disinfection facilities, expansion and rehabilitation of distribution systems and any other water supply, sanitation and drainage work as necessary.

2. Design and supervision of rehabilitation of WTWs, transmission pipelines, and pumping stations, for new chlorinators and tanks, and distribution system expansion and rehabilitation and any other water supply, sanitation and drainage work as necessary.

3. Provision of technical advisory services to carry out feasibility, design, and environmental assessment studies for additional bulk water supplies for Maputo and the four cities.

Part C: Urban Water Supply Policy and Strategy

1. Provision of technical advisory services for the establishment of CRA.

2. Provision of vehicles to CRA.

3. Provision of technical advisory services to assist the Borrower in determining its policy and strategy for further development of urban water supply and sanitation services, including the strategy, design and documentation for the next stage of private sector management for Beira, Quelimane, Nampula and Pemba, and for other eight provincial cities.

4. Provision of technical advisory services to carry out community consultation, design and education programs.

5. Provision of technical advisory services and provision of goods, equipment and logistical assistance to DNA in the management of this Part C.

* * *

The Project is expected to be completed by March 31, 2005.

SCHEDULE 3

Procurement and Consultants' Services

Section I. Procurement of Goods and Works

Part A: General

1. Goods shall be procured in accordance with: (a) 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, subject to the modifications thereto set forth in paragraph 2 of this Part A (the Guidelines), and (b) the provisions of the following Parts of this Section I.

2. In paragraphs 1.6 and 1.8 of the Guidelines, the references to "Bank member countries" and "member country" shall be deemed to be references, respectively, to "Participating Countries" and "Participating Country."

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 1 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) Grouping of contracts

To the extent practicable, contracts for goods and works shall be grouped in bid packages estimated to cost \$100,000 equivalent or more each.

(b) 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

Works estimated to cost less than \$250,000 equivalent per contract, up to an aggregate amount not to exceed \$3,400,000 equivalent, and goods estimated to cost less than \$200,000 equivalent per contract, up to an aggregate amount not to exceed \$900,000 equivalent, may be procured under contracts awarded in accordance with the provisions of paragraphs 3.3 and 3.4 of the Guidelines.

2. International or National Shopping

Goods estimated to cost less than \$50,000 equivalent per contract,

up to an aggregate amount not to exceed \$400,000 equivalent, may be procured under contracts awarded on the basis of international or national shopping procedures in accordance with the provisions of paragraphs 3.5 and 3.6 of the Guidelines.

3. Procurement of Minor Works

Works estimated to cost less than \$50,000 equivalent per contract, up to an aggregate amount not to exceed \$800,000 equivalent, may be procured under lump-sum, fixed-price contracts awarded on the basis of quotations obtained from three (3) qualified domestic contractors in response to a written invitation. The invitation shall include a detailed description of the works, including basic specifications, the required completion date, a basic form of agreement acceptable to the 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. Procurement from IAPSO

Goods estimated to cost less than \$100,000 per contract up to an aggregate amount not to exceed \$400,000 may be procured from the Inter-Agency Procurement Services Office of the UNDP in accordance with the provisions of paragraph 3.9 of the Guidelines.

5. Delegated works and goods

All procurement under Part A.1 and A.2 of the Project shall be carried out in accordance with the provisions of paragraph 3.13 (a) of the Guidelines.

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 each contract estimated to cost the equivalent of \$200,000 or more, the procedures set forth in paragraphs 2 and 3 of Appendix 1 to the Guidelines shall apply.

(b) With respect to each contract estimated to cost the equivalent of \$50,000 or more, the following procedures shall apply:

(i) prior to the selection of any supplier under shopping 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 procured under direct contracting or shopping procedures, 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) and 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

1. Consultants' services shall be procured in accordance with: (a) 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, subject to the modifications thereto set forth in paragraph 2 of this Part A (the Consultant Guidelines), and (b) the provisions of the following Parts of this Section II.

2. In paragraph 1.10 of the Consultant Guidelines, the references to "Bank member countries" and "member country" shall be deemed to be references, respectively, to "Participating Countries" and "Participating Country."

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 \$100,000 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 Based on Consultants' Qualifications

Services for experts estimated to cost less than \$50,000 equivalent per contract may be procured under contracts awarded in accordance with the provisions of paragraphs 3.1 and 3.7 of the Consultant Guidelines.

2. Single Source Selection.

Services which are estimated to cost less than \$100,000 equivalent per contract, may, with the Association's prior agreement, be procured in accordance with the provisions of paragraphs 3.8 through 3.11 of the Consultant Guidelines.

3. Individual Consultants.

Services for training and tasks that meet the requirements set forth in Section 5 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 \$200,000 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 \$100,000 or more, but less than the equivalent of \$200,000, 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 \$50,000 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 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

1. The Borrower shall implement the Project in accordance with the Project Implementation Manual, and except as the Association shall otherwise agree, the Borrower shall not amend or waive any provision thereof if, in the opinion of the Association, such amendment or waiver may materially and adversely affect the implementation of the Project.

2. The Minister of MOPH, in conjunction with the National Director of DNA and the FIPAG Board, shall provide overall policy guidance and project oversight.

3. The Borrower, in conjunction with FIPAG, shall furnish to the Association a semi-annual progress report including information on the status of the Project, having regard to Performance Indicators, and based on data from the monitoring system. The report shall include, inter alia: (a) a summary statement on the status of execution of each project activity; and (b) a table showing compliance with project covenants and progress in implementing agreed policy objectives.

4. (a) The Borrower, in conjunction with FIPAG, shall carry out jointly with the Association, a comprehensive annual project implementation review aimed at: (i) documenting progress toward the achievement of objectives; (ii) identifying and resolving obstacles to project implementation; and (iii) adjusting, in agreement with the Association, targets and corresponding programs to reflect progress achieved in the implementation of the Project as of the date of the review, and ensuring responsiveness to changes to effectively achieve the objectives of the Project.

(b) The Borrower shall, not later than four weeks prior to the review referred to in (a) above, furnish to the Association a report, in such detail as the Association shall reasonably request, including an

evaluation of the progress achieved in Project implementation.

(c) Promptly after completing such reviews, the Borrower shall carry out recommendations arising out of said reviews, with due diligence and efficiency and in accordance with appropriate practices, taking into account the Association's comments thereon.

5. The Borrower shall:

(a) maintain policies and procedures adequate to enable it to monitor and evaluate on an ongoing basis, in accordance with the indicators set forth in Schedule 6 to this Agreement, 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, on or about December 31, 2001, a report integrating the results of the monitoring and evaluation activities performed pursuant to paragraph (a) of this Section, on the progress achieved in the carrying out of the Project during the period preceding the date of 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 March 31, 2002 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 views on the matter.

SCHEDULE 5

Special Account

1. For the purposes of this Schedule:

(a) the term "eligible Categories" means, Categories 1, 2 (a), 3 (a), 4 and 5 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 Credit 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 of \$1,000,000 to be withdrawn from the Credit Account and deposited into the Special Account pursuant to paragraph 3 (a) 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.

3. After the Association 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 respective 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 do not exceed the aggregate amount of the Authorized Allocation. On the basis of such request or requests, the Association shall, on behalf of the Borrower, withdraw from the Credit Account and deposit into 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 Association requests for deposits into the respective Special Account at such intervals as the Association shall specify.

(ii) 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 paragraph 4 of this Schedule 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 respective 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. All such deposits shall be withdrawn by the Association from the Credit 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 Association shall reasonably request, furnish to the Association 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 Association shall not be required to make further deposits into any Special Account:

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

(b) 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 the records and accounts for the Special Account;

(c) 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 the provisions of Section 6.02 of the General Conditions; or

(d) once the total unwithdrawn amount of the Credit allocated to the eligible Categories for the Special Account, minus the total amount of all outstanding special commitments entered into by the Association pursuant to Section 5.02 of the General Conditions with respect to the Project related to the Special Account, shall equal the equivalent of twice the amount of the Authorized Allocation for the Special Account. Thereafter, withdrawal from the Credit Account of the remaining unwithdrawn amount of the Credit allocated to the eligible Categories for the Special Account 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.

6. (a) If the Association 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 Association, the

Borrower shall, promptly upon notice from the Association: (A) provide such additional evidence as the Association may request; or (B) deposit into the respective Special Account (or, if the Association shall so request, refund to the Association) an amount equal to the amount of such payment or the portion thereof not so eligible or justified. 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 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 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 paragraph 6 (a), (b) and (c) of this Schedule shall be credited to the Credit Account for subsequent withdrawal or for cancellation in accordance with the relevant provisions of this Agreement, including the General Conditions.

SCHEDULE 6

Performance Indicators

Population (by city, in 000' and in % where applicable)

Total

Connected

Served by standpipes

Unserved

Average per capita production (served population)

Average per capita production (total population)

Water Production and Billing (by city)

Water produced million m3/year

Water billed million m3/year

Unaccounted for Water %

Connections and Standpipes (by city, in 000')

Legal connections beginning of the year

Illegal Connections regularized during the year

New connections built during the year, by category

Connections closed at the beginning of the year

Connections closed at the end of the year

Total active legal connections at the end of the year, and by category:

Total house connections

Yard connections

Non residential connections (Borrower's Agencies)

Non residential connections

Standpipes

Metered connections by diameter of the connection, and by category

(per city, in 000' and %)

Billing (By city, Metical million)

Residential

Non Residential

Borrower's Agencies

Standpipe

