

CONFORMED COPY

LOAN NUMBER 7230-ME

Loan Agreement

(Decentralized Infrastructure Project)

between

**INTERNATIONAL BANK FOR RECONSTRUCTION
AND DEVELOPMENT**

and

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

Dated March 9, 2005

LOAN NUMBER 7230-ME

LOAN AGREEMENT

AGREEMENT, dated March 9, 2005, between INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT (the Bank) and BANCO NACIONAL DE OBRAS Y SERVICIOS PUBLICOS, S.N.C. (the Borrower).

(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 Bank to assist in the financing of the Project, which forms part of an overall strategy of the Borrower to finance selected projects in different States;

(B) by an agreement (the Guarantee Agreement) of even date herewith between the United Mexican States (the Guarantor) and the Bank, the Guarantor has agreed to guarantee the obligations of the Borrower in respect of the loan provided for in Article II of this Agreement (the Loan) and to undertake such other obligations as set forth in the Guarantee Agreement; and

(C) the Bank has relied on the representations and opinion (*Oficio No. 305.VII-092/2004*) dated April 23, 2004, provided by the *Unidad de Crédito Público* of the Guarantor's Secretariat of Finance and Public Credit to the Bank confirming that the Project has been designed and will be carried out in a manner consistent with the provisions of Article 117 (viii) of the Guarantor's Constitution (*Constitución Política de los Estados Unidos Mexicanos*), as amended to the date of this Agreement; and

WHEREAS the Bank has agreed, on the basis, inter alia, of the foregoing, to extend the Loan to the Borrower upon the terms and conditions set forth in this Agreement;

NOW THEREFORE the parties hereto hereby agree as follows:

ARTICLE I

General Conditions; Definitions

Section 1.01. The "General Conditions Applicable to Loan and Guarantee Agreements for Fixed-Spread Loans" of the Bank, dated September 1, 1999, with the modifications set forth below (the General Conditions) constitute an integral part of this Agreement:

Section 2.01 (8) is modified to read as follows:

"8. 'Conversion Date' means, in respect of a Conversion **other than a Conversion under Section 2.10 of the Loan Agreement**, the Interest Payment Date (or, in the case of a Currency Conversion of an unwithdrawn amount of the Loan, such other date as the Bank shall determine) on which the Conversion enters into effect, as further specified in the Conversion Guidelines **and, in respect of a Conversion under Section 2.10 (Automatic Currency Conversion), the date of withdrawal from the Loan Account of the amount in respect of which the Conversion has been requested.**"

Section 2.01 (47) (c) is modified to read as follows:

"(c) upon a Currency Conversion to an Approved Currency of a withdrawn amount of the Loan that shall accrue interest at a variable rate during the Conversion Period, the variable rate of interest applicable to such amount shall be equal to either: (i) the sum of: (A) LIBOR, **or such other base rate as may be agreed by the Borrower and the Bank**, in respect of said Approved Currency; plus (B) the spread to LIBOR **or to such other base rate**, if any, payable by the Bank under the Currency Hedge Transaction relating to said Currency Conversion; or (ii) if the Bank so determines in accordance with the Conversion Guidelines, the interest rate component of the Screen Rate."

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) "CEAG" means *Comisión Estatal del Agua de Guanajuato*, the Eligible State's State Water Commission;

(b) "CNA" means *Comisión Nacional del Agua*, the Guarantor's National Water Commission;

(c) "COMPRANET" means the Guarantor's electronic public bidding system;

(d) "Currency Conversion Letter" means the letter of even date herewith agreed between the Borrower and the Bank, setting forth the terms and conditions of

Currency Conversions under Section 2.10 of this Agreement, as such letter may be amended from time to time by agreement between the Borrower and the Bank;

(e) “Eligible Categories” means Categories (1), (2), (3) and (4) set forth in the table in Part A.1 of Schedule 1 to this Agreement;

(f) “Eligible Expenditures” means the expenditures for goods, works, and consultants’ services referred to in Section 2.02 of this Agreement;

(g) “Eligible State” means the State of Guanajuato, one of the thirty one political subdivisions –*estados*- of the Guarantor which has been selected by the Borrower to participate in the Borrower’s strategy referred in Whereas (A) of this Agreement;

(h) “Eligible State Agreement” means the agreement between the Borrower and the Eligible State referred in Section 3.01 (b) of this Agreement;

(i) “Environmental and Social Manual” means the manual referred to under Section 3.03 (b) of this Agreement;

(j) “Environmental and Social Regulations” means the set of federal and state laws, decrees and regulations listed in Schedule 5 to this Agreement;

(k) “Financial Monitoring Report” or “FMR” means each report prepared in accordance with Section 4.02 of this Agreement.

(l) “HDM4” means Highway Development and Management System 4, a software system for investigating choices in investing in road transport infrastructure;

(m) “Implementation Letter” means the letter of even date herewith from the Borrower to the Bank containing the monitoring indicators of the Project;

(n) “IVEG” means *Instituto de Vivienda del Estado de Guanajuato*, the Eligible State’s Housing Institute;

(o) “Mexican Pesos” means the lawful currency of the Guarantor;

(p) “Minimum Mexican Wage” means the amount set as minimum wage for the different regions in the territory of the Guarantor, established and reviewed, from time to time, by the National Commission on Minimum Wages within the Secretariat of Labor and Social Affairs of the Guarantor;

(q) “Municipality” means any of the forty six administrative divisions of the Eligible State;

(r) “OP 4.12” means the Bank’s Operational Policy 4.12 (Involuntary Resettlement) dated December 2001;

(s) “Operating Regulations” means the regulations referred to under Section 3.03 (a) of this Agreement;

(t) “Participating Municipality” means: (a) for purposes of Part A of the Project, any Municipality with which the Eligible State has entered into, or will enter into, an agreement for the contribution of funds for, a portion of Part A of the Project; (b) for purposes of Part B of the Project, any Municipality with which the Eligible State has entered into, or will enter into, an agreement for the contribution of funds for, a portion of Part B of the Project; and (c) for purposes of Part C of the Project, any Municipality with which the Eligible State has entered into, or will enter into, an agreement for the contribution of land for a portion of Part C of the Project;

(u) “Procurement Law” means: (a) the *Ley de Adquisiciones, Arrendamientos y Servicios del Sector Público*, published in the Guarantor’s Official Gazette on January 4, 2000, as amended to the date of this Agreement; (b) the *Reglamento de la Ley de Adquisiciones, Arrendamientos y Servicios del Sector Público*, published in the Guarantor’s Official Gazette on August 20, 2001, as amended to the date of this Agreement; (c) the *Ley de Obras Públicas y Servicios Relacionados con las mismas*, published in the Guarantor’s Official Gazette on January 4, 2000, as amended to the date of this Agreement; and (d) the *Reglamento de la Ley de de Obras Públicas y Servicios Relacionados con las mismas*, published in the Guarantor’s Official Gazette on August 20, 2001, as amended to the date of this Agreement;

(v) “Procurement of Goods Law” means the *Ley de Adquisiciones, Arrendamientos y Servicios del Sector Público*, published in the Guarantor’s Official Gazette on January 4, 2000, as amended to the date of this Agreement;

(w) “Procurement of Works Law” means the *Ley de Obras Públicas y Servicios Relacionados con las mismas*, published in the Guarantor’s Official Gazette on January 4, 2000, as amended to the date of this Agreement;

(x) “Procurement Plan” means the procurement plan for the Project, to be provided by the Borrower to the Bank prior to the Effective Date covering the initial 18 month period (or longer) of Project implementation, as the same shall be updated from time to time in accordance with the provisions of Section 3.02 (b) to this Agreement, to cover succeeding 18 month periods (or longer) of Project implementation;

(y) “Report-based Disbursements” means the disbursement modality referred to in paragraph 4 of Part A of Schedule 1 to this Agreement;

(z) “SAP R/3” means the budget and financial information system of the Eligible State;

(aa) “SHCP” means *Secretaría de Hacienda y Crédito Público*, the Guarantor’s Finance and Public Credit Secretariat; and

(ab) “SOP” means *Secretaría de Obras Públicas*, the Public Works Secretariat of the Eligible State.

ARTICLE II

The Loan

Section 2.01. The Bank agrees to lend to the Borrower, on the terms and conditions set forth or referred to in this Agreement, an amount equal to one hundred eight million Dollars (\$108,000,000), as such amount may be converted from time to time through a Currency Conversion in accordance with the provisions of Section 2.09 and 2.10 of this Agreement.

Section 2.02. The amount of the Loan may be withdrawn from the Loan Account in accordance with the provisions of Schedule 1 to this Agreement for expenditures made (or, if the Bank shall so agree, to be made) in respect of goods, works and services required for the Project and to be financed out of the proceeds of the Loan, and in respect of any premium in respect of an Interest Rate Cap or Interest Rate Collar payable by the Borrower in accordance with Section 4.04(c) of the General Conditions, provided however, that no Loan proceeds may be used for the payment of any premium for an Interest Rate Cap or Interest Rate Collar until the Bank has allowed this option by written notice to the Borrower and, accordingly, until such written notice has been sent by the Bank to the Borrower, the Borrower shall finance said premia for Interest Rate Caps or Interest Rate Collars, if any, with its own funds.

Section 2.03. The Closing Date shall be December 31, 2008 or such later date as the Bank shall establish. The Bank shall promptly notify the Borrower and the Guarantor of such later date.

Section 2.04. (a) The Borrower shall pay to the Bank a front-end fee in an amount equal to one percent (1%) of the amount of the Loan. Such fee shall be payable not later than sixty (60) days after the Effective Date.

Section 2.05. The Borrower shall pay to the Bank a commitment charge on the principal amount of the Loan not withdrawn from time to time, at a rate equal to: (i) eighty five one-hundredths of one per cent (0.85%) per annum from the date on which such charge commences to accrue in accordance with the provisions of Section 3.02 of the General Conditions to but not including the fourth anniversary of such date; and (ii) seventy five one-hundredths of one per cent (0.75%) per annum thereafter.

Section 2.06. The Borrower shall pay interest on the principal amount of the Loan withdrawn and outstanding from time to time, in respect of each Interest Period, at the Variable Rate; provided that, upon a Conversion of all or any portion of the principal amount of the Loan, the Borrower shall, during the Conversion Period, pay interest on such amount in accordance with the relevant provisions of Article IV of the General Conditions.

Section 2.07. Interest and commitment charges shall be payable semiannually in arrears on August 1 and February 1 in each year.

Section 2.08. The Borrower shall repay the principal amount of the Loan in accordance with the provisions of Schedule 3 to this Agreement.

Section 2.09. (a) The Borrower may at any time request any of the following Conversions of the terms of the Loan in order to facilitate prudent debt management:

- a change of the Loan Currency of all or any portion of the principal amount of the Loan, withdrawn or unwithdrawn, to an Approved Currency;

- a change of the interest rate basis applicable to all or any portion of the principal amount of the Loan from a Variable Rate to a Fixed Rate, or vice versa; and

- the setting of limits on the Variable Rate applicable to all or any portion of the principal amount of the Loan withdrawn and outstanding by the establishment of an Interest Rate Cap or Interest Rate Collar on said Variable Rate.

(b) Any conversion requested pursuant to paragraph (a) of this Section that is accepted by the Bank shall be considered a “Conversion”, as defined in Section 2.01(7) of the General Conditions, and shall be effected in accordance with the provisions of Article IV of the General Conditions and of the Conversion Guidelines.

(c) Subject to the proviso in Section 2.02 of the Agreement, promptly following the Execution Date for an Interest Rate Cap or Interest Rate Collar in respect of which the Borrower has requested that the premium be paid out of the proceeds of the Loan, the Bank shall, on behalf of the Borrower, withdraw from the Loan Account and pay to itself the amounts required to pay any premium payable in accordance with Section 4.04(c) of the General Conditions up to the amount allocated from time to time for such purpose in the table in paragraph 1 of Schedule 1 to this Agreement.

Section 2.10. Without limitation upon the provisions of paragraph (a) of Section 2.09 of this Agreement and unless otherwise notified by the Borrower to the Bank in accordance with the provisions of the Conversion Guidelines, any amount withdrawn from the Loan Account shall be converted from Dollars to Mexican Pesos (MXN) for the full maturity of such amount with effect from the Conversion Date, such Conversion to be carried out in accordance with the terms and conditions of the Currency Conversion Letter.

Section 2.11. The *Director de Finanzas* of BANOBRAS and any person or persons whom he or she shall designate in writing is designated as representative of the Borrower for the purposes of taking any action required or permitted to be taken under the provisions of Section 2.02 of this Agreement and Article V 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 as set forth in Schedule 2 to this Agreement, and, to this end shall: (i) cause the Eligible State to carry out the Project; and (ii) provide, or cause the Eligible State to provide, in a timely manner and as needed, the funds, facilities, services and other resources required for the Project, all of the above with due diligence and efficiency and in conformity with appropriate administrative, financial, technical, auditing, environmental and social standards and practices on the part of both the Borrower and the Eligible State.

(b) The Borrower shall lend the proceeds of the Loan to the Eligible State under the particular terms of a loan agreement to be entered into between the Borrower and the Eligible State (*contrato de apertura de crédito simple*), which terms and conditions shall have been approved by the Bank and shall include, *inter alia*,

- (i) the agreement of the Eligible State to:
 - (A) carry out the Project in accordance with the terms and conditions of this Agreement (including its Schedules), the Operating Regulations, the Environmental and Social Policies and Regulations, the Environmental and Social Manual, the Implementation Letter and OP 4.12 (the latter, if applicable under Section 3.04 below), including the obligation of the Eligible State to carry out Part C.1 of the Project by not later than January 1, 2006;
 - (B) enter into the agreements that may correspond with the Guarantor (through CNA), and the Participating Municipalities to regulate the financial contributions, if any, to be made by the Guarantor and the Participating Municipalities for the financing of the Project;
 - (C) enter into the required arrangements with CEAG, IVEG and SOP to regulate CEAG's, IVEG's and SOP's participation in the execution and financing of the Project, said arrangements to be satisfactory to the Bank and to include, *inter alia*,
 - (1) the obligation of CEAG, IVEG and SOP to, *inter alia*:
 - 1. carry out the Project in accordance with the terms and conditions of this Agreement (including its Schedules), the Operating Regulations, the Environmental and Social Policies and Regulations, the Environmental and Social Manual, the Implementation Letter, and OP 4.12 (the latter, if applicable under Section 3.04 below);
 - 2. keep records and accounts for the expenditures financed under the Project;
 - 3. collaborate with the Eligible State to allow the Eligible State's compliance of

its obligations under the Eligible State Agreement; and

4. enable the Borrower to review CEAG's, IVEG's and SOP's accounts that relate to the Project, and provide other information as the Borrower shall request in respect of the Project; and

(2) the Eligible State's right to suspend the transfer of funds under the arrangements with CEAG, IVEG or SOP, in case of noncompliance by CEAG, IVEG or SOP of any of their obligations under their respective arrangements, as the case maybe;

(D) to submit to the Borrower:

(1) a list of, and all relevant information related to the activities that, according to criteria set forth in the Environmental and Social Manual, need to be reviewed by the Bank prior to their execution;

(2) not later than October 1 of each year, an annual work program for the Bank's review containing the specific Project activities to be carried out during the immediate following year, the costs of those activities, the sources of financing of those activities (including Loan proceeds and other funds provided by the Eligible State) and the institutional strengthening measures to be carried out under Part D.3 of the Project during said year; and

(3) all information related to the implementation and monitoring of the Project (including, but not limited to, the information required to prepare the report referred to in Section 3.06 (b) of this Agreement and the plan referred to in Section 3.07 (a) of this Agreement, and the information

listed under Article IV of this Agreement and Schedules 1 and 4 of this Agreement);

- (E) to keep records and accounts for the expenditures financed under the Project;
 - (F) to enable the Borrower to review the Eligible State's accounts that relate to the Project, and provide to the Borrower any other information as the Bank shall reasonably request in respect of the Project; and
 - (G) to comply with the obligations set forth in Sections 9.04, 9.05, 9.06, 9.07, 9.08 and 9.09 of the General Conditions (relating to insurance, use of goods and services, plans and schedules, records and reports, maintenance and land acquisition, respectively);
- (ii) the Borrower's obligation to transfer the Loan proceeds to the Eligible State for the execution of the Project;
 - (iii) the Borrower's right to suspend disbursements under the Eligible State Agreement in case of non-compliance by the Eligible State of its obligations under such Eligible State Agreement;
 - (iv) the Borrower's right to cancel an amount from the loan to the Eligible State under the Eligible State Agreement equivalent to the amount cancelled by the Bank from the Loan pursuant to Sections 3.02 (c), (d), (e) and (f) of this Agreement;
 - (v) the criteria for the selection of the roads to be rehabilitated, improved or maintained under Part A.1 of the Project; and
 - (vi) the maximum loan amount, selection criteria, collateral and other regulations for housing loans under Part C.2 of the Project.

(c) The Borrower shall promptly notify the Bank in case of an event of non-compliance by the Eligible State with the terms and conditions of the Eligible State Agreement, the Operating Regulations, the Environmental and Social Policies and Regulations, the Environmental and Social Manual or the Implementation Letter; and

(d) The Borrower shall exercise its rights under the Eligible State Agreement in such a manner as to protect the interests of the Borrower and the Bank and to accomplish the purposes of the Loan, and, except as the Bank shall otherwise agree, the Borrower shall not assign, amend, abrogate, waive or fail to enforce the Eligible State Agreement or any provision thereof. In case of any conflict between the terms of the Eligible State Agreement and those of this Agreement, the terms of this Agreement shall prevail.

Section 3.02. (a) Except as the Bank shall otherwise agree, procurement of the goods, works and consultants' services required for the Project and to be financed out of any sources of financing shall be governed by the provisions of Schedule 4 to this Agreement, as said provisions may be further elaborated in the Procurement Plan.

(b) The Borrower shall update the Procurement Plan in accordance with terms of reference acceptable to the Bank, and furnish such update to the Bank not later than 12 months after the date of the preceding Procurement Plan, for the Bank's approval.

(c) Without prejudice to the provisions of Section 6.03 (d) of the General Conditions (and as a supplement to the terms of paragraph 1.12 of the Guidelines referred to in Schedule 4 to this Agreement and paragraph 1.17 of the Consultant Guidelines also referred to in said Schedule), if, at any time, the Bank determines that the procurement of any contract financed or to be financed from any sources of financing to carry out Part A of the Project is inconsistent with the procedures set forth or referred to in this Agreement, the Bank may, by notice to the Borrower, terminate the right of the Borrower to make withdrawals with respect to fifty five percent (55%) of the amount of expenditures in respect of such contract. Upon the giving of such notice, such amount of the Loan shall be cancelled.

(d) Without prejudice to the provisions of Section 6.03 (d) of the General Conditions (and as a supplement to the terms of paragraph 1.12 of the Guidelines referred to in Schedule 4 to this Agreement and paragraph 1.17 of the Consultant Guidelines also referred to in said Schedule), if, at any time, the Bank determines that the procurement of any contract financed or to be financed from any sources of financing to carry out Part B of the Project is inconsistent with the procedures set forth or referred to in this Agreement, the Bank may, by notice to the Borrower, terminate the right of the Borrower to make withdrawals with respect to forty five percent (45%) of the amount of expenditures in respect of such contract. Upon the giving of such notice, such amount of the Loan shall be cancelled.

(e) Without prejudice to the provisions of Section 6.03 (d) of the General Conditions (and as a supplement to the terms of paragraph 1.12 of the Guidelines referred to in Schedule 4 to this Agreement and paragraph 1.17 of the Consultant Guidelines also referred to in said Schedule), if, at any time, the Bank determines that the procurement of

any contract financed or to be financed from any sources of financing to carry out Part C of the Project is inconsistent with the procedures set forth or referred to in this Agreement, the Bank may, by notice to the Borrower, terminate the right of the Borrower to make withdrawals with respect to a hundred percent (100%) of the amount of expenditures in respect of such contract. Upon the giving of such notice, such amount of the Loan shall be cancelled.

(f) Without prejudice to the provisions of Section 6.03 (d) of the General Conditions (and as a supplement to the terms of paragraph 1.12 of the Guidelines referred to in Schedule 4 to this Agreement and paragraph 1.17 of the Consultant Guidelines also referred to in said Schedule), if, at any time, the Bank determines that the procurement of any contract financed or to be financed from any sources of financing to carry out Part D of the Project is inconsistent with the procedures set forth or referred to in this Agreement, the Bank may, by notice to the Borrower, terminate the right of the Borrower to make withdrawals with respect to a hundred percent (100%) of the amount of expenditures in respect of such contract. Upon the giving of such notice, such amount of the Loan shall be cancelled.

Section 3.03. Without limitation upon the provision of Section 3.01 (a) above, and except as the Bank shall otherwise agree, the Borrower shall cause the Eligible State to carry out the Project in accordance with:

(a) operating regulations, satisfactory to the Bank, which shall contain, *inter alia*, the procedures for the carrying out, monitoring and evaluation of the Project (including the procurement and financial requirements thereof, such as a procurement plan model and criteria for financial management);

(b) an environmental and social manual, satisfactory to the Bank, which shall contain, *inter alia*,

- (i) the norms and procedures to screen the environmental and social impacts of the different activities under the Project;
- (ii) the norms and procedures to assess the environmental and social compliance capacity of the agencies in charge of executing and monitoring the different activities under the Project;
- (iii) a system to identify activities under the Project that need to be submitted to the Bank for the Bank's review prior to their execution (together with the relevant environmental or social assessment and the corresponding mitigation measures); and

- (iv) a plan listing the institutional strengthening activities to be carried out under Part D.3 of the Project during the first year of Project implementation;
- (c) the environmental and social regulations listed in Schedule 5 to this Agreement, said Environmental and Social Regulations not to be amended for purposes of the Project without the Bank's agreement;
- (d) the Implementation Letter; and
- (e) the annual work program referred to in Section 3.01 (b) (i) (D) (2) above.

In case of conflict between the terms of this Agreement and those of the Operating Regulations or the Environmental and Social Manual, the terms of this Agreement shall prevail. In case of conflict between the terms of the Operating Regulations and those of the Environmental and Social Manual, the terms of the Environmental and Social Manual shall prevail.

Section 3.04. Notwithstanding Section 3.03 (b) and (c) above, if under any Part of the Project, a situation arises in which a person or a group of people need to be resettled, the Bank may, at its own discretion, apply the procedures set forth under OP 4.12 and require the Borrower to carry out and cause the Eligible State to carry out all the actions resulting from the application of said OP 4.12.

Section 3.05. Without limitation to Section 3.01 (a) above, the Borrower shall:

- (a) submit to the Bank a list of the activities that, according to criteria set forth in the Environmental and Social Manual, need to be reviewed by the Bank prior to their execution; and
- (b) provide the Bank all the information that the Bank shall reasonably request with respect to the Project, including all information related to the accounts of CEAG, IVEG and SOP related to the Project.

Section 3.06. Without limitation to Section 3.01 (a) above, the Borrower shall:

- (a) maintain policies and procedures adequate to enable it to monitor and evaluate on an ongoing basis, in accordance with the monitoring indicators set forth in the Implementation Letter, the carrying out of the Project and the achievement of the objectives thereof;

(b) not later than November 1 of each year, submit to the Bank the annual work program referred to in Section 3.01 (b) (i) (D) (2) above for the Bank's review;

(c) prepare, under terms of reference satisfactory to the Bank, and furnish to the Bank upon the Bank's request a report integrating the results of the monitoring and evaluation activities performed pursuant to paragraph (a) of this Section, on the progress achieved in the carrying out of the Project during the period preceding the date of such report (based on the annual work program provided to the Bank pursuant to paragraph (b) of this Section) 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

(d) (i) review with the Bank each report referred to in paragraph (c) of this Section, within no more than two months after each such report's delivery to the Bank; and

(ii) 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 reports and the Bank's views on the matter.

Section 3.07. 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 Bank, and furnish to the Bank not later than six (6) months after the Closing Date or such later date as may be agreed for this purpose between the Borrower and the Bank, a plan designed to ensure the sustainability of the Project; and

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

ARTICLE IV

Financial Covenants

Section 4.01. (a) The Borrower shall cause the Eligible State (including CEAG, IVEG and SOP and the Participating Municipalities) to establish and maintain a financial management system, including records and accounts, and prepare financial statements in accordance with consistently applied accounting standards acceptable to the Bank,

adequate to reflect the operations, resources and expenditures related to the Project (regardless of whether said expenditures are financed with Loan proceeds or with any other sources of financing).

(b) The Borrower shall cause the Eligible State (including CEAG, IVEG and SOP and the Participating Municipalities) to:

- (i) have the financial statements referred to in paragraph (a) of this Section for each fiscal year (or other period agreed to by the Bank) audited, in accordance with consistently applied auditing standards acceptable to the Bank, by independent auditors acceptable to the Bank;
- (ii) furnish to the Borrower for the Borrower to submit to the Bank as soon as available, but in any case not later than six months after the end of each such year (or such other period agreed to by the Bank): (A) certified copies of the financial statements referred to in paragraph (a) of this Section for such year (or other period agreed to by the Bank), as so audited; and (B) an opinion on such statements by said auditors, in scope and detail satisfactory to the Bank (including an opinion on the evidence used to document the percentages referred to in paragraphs 2 (d), 2 (e), 2 (f), and 2 (g) of Part A of Schedule 1 to this Agreement); and
- (iii) furnish to the Borrower for the Borrower to submit to the Bank such other information concerning such records and accounts, and the audit of such financial statements, and concerning said auditors, as the Bank may from time to time reasonably request.

(c) For all expenditures with respect to which withdrawals from the Loan Account were made on the basis of the reports referred to in Part A.4 of Schedule 1 to this Agreement (Report-based Disbursements) or statements of expenditure as well as for all expenditures financed from sources other than Loan proceeds, the Borrower shall:

- (i) retain, until at least one year after the Bank has received the audit report for, or covering, the fiscal year in which the last withdrawal from the Loan Account was made, all records (contracts, orders, invoices, bills, receipts and other documents) evidencing such expenditures;
- (ii) enable the Bank's representatives to examine such records; and

- (iii) ensure that such reports, statements of expenditure and the evidence of expenditures financed from sources other than Loan proceeds are included in the audit for each fiscal year (or other period agreed to by the Bank), referred to in paragraph (b) of this Section.

(d) The Borrower shall furnish to the Bank as soon as available, but in any case not later than six months after the end of each such year (or such other period agreed to by the Bank): (A) certified copies of the financial statements referred to in paragraph (a) of this Section for such year (or other period agreed to by the Bank), as so audited; and (B) an opinion on such statements by said auditors, in scope and detail satisfactory to the Bank (including an opinion on the evidence used to document the percentages referred to in paragraphs 2 (d), 2 (e), 2 (f), and 2 (g) of Part A of Schedule 1 to this Agreement); and

(e) The Borrower shall furnish to the Bank such other information concerning such records and accounts, and the audit of such financial statements, and concerning said auditors, as the Bank may from time to time reasonably request.

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

- (i) sets forth sources and uses of funds for the Project, both cumulatively and for the period covered by said report, showing separately funds provided under the Loan, and explains variances between the actual and planned uses of such funds;
- (ii) describes physical progress in Project implementation, both cumulatively and for the period covered by said report, including progress in achievement of the output indicators set forth in Schedule 6 to this Agreement and the related disbursement eligibility calculation, and explains variances between the actual and planned Project implementation; and
- (iii) sets forth the status of procurement under the Project, as at the end of the period covered by said report.

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

ARTICLE V

Remedies of the Bank

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

(a) the Eligible State shall have failed to perform any of its obligations under the Eligible State Agreement or a situation shall have arisen so as to materially and adversely affect, in the opinion of the Bank, the ability of the Eligible State to carry out its obligations under the Eligible State Agreement; and

(b) any of the Participating Municipalities, CEAG, IVEG or SOP shall have failed to perform any of its obligations under the relevant agreement or arrangements, as the case may be, or a situation shall have arisen so as to materially and adversely affect, in the opinion of the Bank, the ability of any of the Participating Municipalities, CEAG, IVEG or SOP to carry out their respective obligations under the relevant agreement or arrangement.

Section 5.02. Pursuant to Section 7.01(k) of the General Conditions, the following additional event is specified; namely, that any event specified in paragraph (a) of Section 5.01 of this Agreement shall occur and shall continue for a period of sixty (60) days after notice thereof shall have been given by the Bank to the Borrower.

ARTICLE VI

Effective Date; Termination

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

(a) that the Eligible State Agreement has been entered into by the Borrower and the Eligible State;

(b) that the Environmental and Social Manual has been furnished to the Bank by the Borrower;

(c) that the Operating Regulations have been furnished to the Bank by the Borrower; and

(d) that a procurement plan, satisfactory to the Bank, covering the initial 18 month period (or longer) of Project implementation has been furnished by the Borrower to the Bank.

Section 6.02. The following is specified as an additional matter, within the meaning of Section 12.02 (c) of the General Conditions, to be included in the opinion or opinions to be furnished to the Bank, namely, that the Borrower (in its legal opinion) and the Eligible State (in a separate legal opinion satisfactory to the Bank, issued by the Eligible State counsel acceptable to the Bank), indicate that the Eligible State Agreement has been duly authorized or ratified by, and executed and delivered on behalf of, the Borrower and the Eligible State and is legally binding upon the Borrower and the Eligible State in accordance with the Eligible State Agreement's terms.

Section 6.03. The date June 7, 2005 is hereby specified for the purposes of Section 12.04 of the General Conditions.

ARTICLE VII

Representative of the Borrower; Addresses

Section 7.01. Except as provided in Section 2.11 of this Agreement, the *Subdirector de Planeación y Programación* 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:

Avenida Javier Barros Sierra 515, piso 8
Colonia Lomas de Santa Fe, Delegación Alvaro Obregón
México, D.F. 01219
México

Facsimile:

011-52-55 5270-1633

For the Bank:

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

Cable address:

Telex:

Facsimile:

INTBAFRAD
Washington, D.C.

248423 (MCI) or
64145 (MCI)

(202) 477-6391

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

INTERNATIONAL BANK FOR
RECONSTRUCTION AND DEVELOPMENT

By /s/ Isabel Guerrero

Authorized Representative

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

By /s/ Verónica Baranda Sepúlveda

Authorized Representative

SCHEDULE 1

Withdrawal of the Proceeds of the Loan

Part A

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

<u>Category</u>	<u>Amount of the Loan Allocated (expressed in Dollars)</u>	<u>% of Expenditures To be Financed</u>
(1) Goods, Works and Services (other than Consultants' Services) and Consultants Services under Part A of the Project	59,000,000	55%
(2) Goods, Works and Services (other than Consultants' Services) and Consultants Services under Part B of the Project	38,000,000	45%
(3) Goods, Works and Services (other than Consultants' Services) and Consultants Services under Part C of the Project	7,000,000	100%
(4) Goods, Works and Services (other than Consultants' Services) and Consultants Services under Part D of the Project	1,500,000	100%

(5)	Premia for Interest Rate Caps and Interest Rate Collars	- 0 -	Amount due under Section 2.09 (c) of this Agreement
(6)	Unallocated	2,500,000	
	TOTAL	<u>108,000,000</u>	

2. Notwithstanding the provisions of paragraph 1 above, no withdrawals shall be made:

(a) in respect of any Category set forth in the table in paragraph 1 of Part A of this Schedule unless and until the Borrower shall have paid to the Bank in full the front-end fee referred to in Section 2.04 of this Agreement;

(b) in respect of payments made for expenditures prior to the date of this Agreement, except that withdrawals, in an aggregate amount not exceeding \$10,800,000 may be made in respect of Categories (1), (2), (3) and (4) set forth in the table in paragraph 1 of Part A of this Schedule on account of payments made for expenditures incurred up to twelve months prior to the date of this Agreement;

(c) in respect of any Category set forth in the table in paragraph 1 of Part A of this Schedule, unless: (i) the Borrower has submitted evidence satisfactory to the Bank of achievement of one or more of the outputs listed in Schedule 6 to this Agreement, provided that said outputs have not already been claimed by the Borrower to support previous withdrawal applications from the Loan Account; and (ii) the amount to be so withdrawn is less than or equal to the sum of the amounts assigned under Schedule 6 to each of the outputs identified by the Borrower pursuant to subparagraph 2 (c) (i) above and accepted by the Bank as the basis for the relevant withdrawal; all of this, provided, however that: (A) if under exceptional circumstances the amount that the Borrower is entitled to withdraw on the basis of subparagraphs 2 (c) (i) and 2 (c) (ii) above would not provide sufficient funds for an adequate execution of the Project, the Bank may, by notice in writing to the Borrower, temporarily waive compliance with said subparagraphs 2 (c) (i) and 2 (c) (ii); and (B) this paragraph (c) shall not apply to: (1) the first withdrawal from the Special Account referred under paragraph 4 *in fine* of Part B of this Schedule 1 (when the Borrower is making Report-based disbursements); and (2) the first \$10,000,000 equivalent to be withdrawn from the Loan Account for deposit into the Special Account (when the Borrower is not making Report-based disbursements);

(d) in respect of payments covered by Category (1) set forth in the table in paragraph 1 of this Part A, in the event the Borrower shall have failed to furnish to the

Bank by a date six months after the end of each fiscal year, together with the audits referred to in Section 4.01 (b) of this Agreement, such documents and other evidence showing, to the satisfaction of the Bank, that at least 55% of the expenditures under Part A of the Project financed with Loan Proceeds and other sources of funding and covered by Category (1) set forth in the table in paragraph 1 of this Part A were used for goods, works, services and incremental operating costs, eligible for financing out of the proceeds of the Loan as confirmed by such audit report;

(e) in respect of payments covered by Category (2) set forth in the table in paragraph 1 of this Part A, in the event the Borrower shall have failed to furnish to the Bank by a date six months after the end of each fiscal year, together with the audits referred to in Section 4.01 (b) of this Agreement, such documents and other evidence showing, to the satisfaction of the Bank, that at least 45% of the expenditures under Part B of the Project financed with Loan Proceeds and other sources of funding and covered by Category (2) set forth in the table in paragraph 1 of this Part A were used for goods, works, services and incremental operating costs, eligible for financing out of the proceeds of the Loan as confirmed by such audit report;

(f) in respect of payments covered by Category (3) set forth in the table in paragraph 1 of this Part A, in the event the Borrower shall have failed to furnish to the Bank by a date six months after the end of each fiscal year, together with the audits referred to in Section 4.01 (b) of this Agreement, such documents and other evidence showing, to the satisfaction of the Bank, that at least 100% of the expenditures under Part C of the Project financed with Loan Proceeds and other sources of funding and covered by Category (3) set forth in the table in paragraph 1 of this Part A were used for goods, works, services and incremental operating costs, eligible for financing out of the proceeds of the Loan as confirmed by such audit report; and

(g) payments covered by Category (4) set forth in the table in paragraph 1 of this Part A, in the event the Borrower shall have failed to furnish to the Bank by a date six months after the end of each fiscal year, together with the audits referred to in Section 4.01 (b) of this Agreement, such documents and other evidence showing, to the satisfaction of the Bank, that at least 83% of the expenditures under Part D of the Project financed with Loan Proceeds and other sources of funding and covered by Category (4) set forth in the table in paragraph 1 of this Part A were used for goods, works, services and incremental operating costs, eligible for financing out of the proceeds of the Loan as confirmed by such audit report.

3. The Bank may require withdrawals from the Loan Account to be made on the basis of statements of expenditure for goods, works and services required under the Project; all of these under such terms and conditions as the Bank shall specify by notice to the Borrower.

4. The Bank may require withdrawals from the Loan Account to be made on the basis of reports to be submitted to the Bank in form and substance satisfactory to the Bank, such reports to include the FMR and any other information as the Bank shall specify by notice to the Borrower (Report-based Disbursements), including the outputs achieved (as referred to in Schedule 6 to this Agreement). In the case of the first such request submitted to the Bank for deposit into the Special Account, the Borrower shall submit to the Bank only a statement with the projected sources and applications of funds for the Project for the six-month period following the date of such request.

B. Special Account

1. The Borrower shall open and maintain in Mexican Pesos a special deposit account in a commercial bank acceptable to the Bank, on terms and conditions satisfactory to the Bank, including appropriate protection against set-off, seizure and attachment.

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

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

(b) if the Borrower is making Report-based Disbursements, withdrawals shall be made in accordance with the provisions of Annex B to this Schedule 1.

3. Payments out of the Special Account shall be made exclusively for Eligible Expenditures. For each payment made by the Borrower out of the Special Account, the Borrower shall, at such time as the Bank shall reasonably request, furnish to the Bank such documents and other evidence showing that such payment was made exclusively for Eligible Expenditures.

4. Notwithstanding the provisions of Part B.2 of this Schedule, the Bank shall not be required to make further deposits into the Special Account:

(a) if the Bank, at any time, is not satisfied that the reports referred to in Part A. 4 of this Schedule 1 adequately provide the information required for Report-based Disbursements;

(b) if the Bank determines at any time that all further withdrawals for payment of Eligible Expenditures should be made by the Borrower directly from the Loan Account; or

(c) if the Borrower shall have failed to furnish to the Bank, within the period of time specified in Section 4.01 (b) (ii) of this Agreement, any of the audit reports required to be furnished to the Bank pursuant to said Section in respect of the audit of: (A) the records and accounts for the Special Account; or (B) the records and accounts reflecting expenditures with respect to which withdrawals were Report-based Disbursements or were made on the basis of statements of expenditure, as the case may be.

5. The Bank shall not be required to make further deposits into the Special Account in accordance with the provisions of Part B.2 of this Schedule if, at any time, the Bank shall have notified the Borrower and the Guarantor of its intention to suspend in whole or in part the right of the Borrower to make withdrawals from the Loan Account pursuant to Section 6.02 of the General Conditions. Upon such notification, the Bank shall determine, in its sole discretion, whether further deposits into the Special Account may be made and what procedures should be followed for making such deposits, and shall notify the Borrower and the Guarantor of its determination.

6. (a) If the Bank determines at any time that any payment out of the Special Account was made for an expenditure which is not an Eligible Expenditure, or was not justified by the evidence furnished to the Bank (including, but not limited to, the evidence referred to in paragraphs 2 (d), (e), (f) and (g) of Part A of this Schedule, and the evidence related to physical outputs referred to in paragraph 2 (c) of Part A of this Schedule), the Borrower shall, promptly upon notice from the Bank, provide such additional evidence as the Bank may request, or deposit into the Special Account (or, if the Bank shall so request, refund to the Bank) an amount equal to the amount of such payment. Unless the Bank shall otherwise agree, no further deposit by the Bank into the Special Account shall be made until the Borrower has provided such evidence or made such deposit or refund, as the case may be.

(b) If the Bank determines at any time that any amount outstanding in the Special Account will not be required to cover payments for Eligible Expenditures during the six-month period following such determination, the Borrower shall, promptly upon notice from the Bank, refund to the Bank such outstanding amount.

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

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

Annex A

to

SCHEDULE 1

**Operation of Special Account
When Withdrawals Are Not
Report-based Disbursements**

1. For the purposes of this Annex, the term “Authorized Allocation” means the amount of \$10,000,000 to be withdrawn from the Loan Account and thereafter deposited in Mexican Pesos into the Special Account pursuant to paragraph 2 of this Annex, provided, however, that an amount higher than \$10,000,000 equivalent may at any point be contained in the Special Account, but only as a consequence of exchange rate fluctuations between the Dollar and the Mexican Peso subsequent to the deposit of the Authorized Allocation in the Special Account.

2. Withdrawals of the Authorized Allocation and subsequent withdrawals to replenish the Special Account shall be made as follows:

(a) For withdrawals of the Authorized Allocation, the Borrower shall furnish to the Bank a request or requests for deposit into the Special Account of an amount or amounts which in the aggregate do not exceed the Authorized Allocation. On the basis of each such request, the Bank shall, on behalf of the Borrower, withdraw from the Loan Account and deposit into the Special Account such amount as the Borrower shall have requested.

(b) For replenishment of the Special Account, the Borrower shall furnish to the Bank requests for deposit into the Special Account at such intervals as the Bank shall specify. Prior to or at the time of each such request, the Borrower shall furnish to the Bank the documents and other evidence required pursuant to Part B.3 of Schedule 1 to this Agreement for the payment or payments in respect of which replenishment is requested. On the basis of each such request, the Bank shall, on behalf of the Borrower, withdraw from the Loan Account and deposit into the Special Account such amount as the Borrower shall have requested and as shall have been shown by said documents and other evidence to have been paid out of the Special Account for Eligible Expenditures. Each such deposit into the Special Account shall be withdrawn by the Bank from the Loan Account under one or more of the Eligible Categories.

3. The Bank shall not be required to make further deposits into the Special Account, once the total unwithdrawn amount of the Loan minus the total amount of all outstanding

special commitments entered into by the Bank pursuant to Section 5.02 of the General Conditions shall equal the equivalent of twice the amount of the Authorized Allocation.

Thereafter, withdrawal from the Loan Account of the remaining unwithdrawn amount of the Loan shall follow such procedures as the Bank shall specify by notice to the Borrower. Such further withdrawals shall be made only after and to the extent that the Bank shall have been satisfied that all such amounts remaining on deposit in the Special Account as of the date of such notice will be utilized in making payments for Eligible Expenditures.

4. Paragraph 2 (c) of Part A of this Schedule 1 shall not apply to the first \$10,000,000 equivalent to be withdrawn from the Loan Account for deposit into the Special Account.

Annex B

to

SCHEDULE 1

**Operation of Special Account
When Withdrawals Are
Report-based Disbursements**

1. Withdrawals from the Loan Account shall be deposited by the Bank into the Special Account in accordance with the provisions of Schedule 1 to this Agreement. Each such deposit into the Special Account shall be withdrawn by the Bank from the Loan Account under one or more of the Eligible Categories.

2. Upon receipt of each application for withdrawal of an amount of the Loan, the Bank shall, on behalf of the Borrower, withdraw from the Loan Account and deposit into the Special Account an amount equal to the lesser of: (a) the amount so requested; and (b) the amount which the Bank has determined, based on the reports referred to in Part A. 4 of this Schedule 1 applicable to such withdrawal application, is required to be deposited in order to finance Eligible Expenditures during the six-month period following the date of such reports; provided, however, that the amount so deposited, when added to the amount indicated by said Financial Monitoring Report to be remaining in the Special Account, shall not exceed, \$27,000,000 equivalent as of the date of each deposit into the Special Account (regardless of whether, due to subsequent exchange rate fluctuations between the Dollar and the Mexican Peso, an amount higher than \$27,000,000 equivalent may result to be remaining in the Special Account).

SCHEDULE 2

Description of the Project

The objective of the Project is to improve the provision and performance of infrastructure services in the Eligible State.

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

Part A: Roads

1. Rehabilitation, improvement and maintenance of selected segments of the approximately 2,600 km of roads subject to rehabilitation, improvement and maintenance by the Eligible State, including widening of shoulders, provision of adequate drainage, strengthening of bridges, and provision of road signs and other safety measures and the provision of technical assistance to foster the creation of micro-enterprises to carry out the referred maintenance.

2. Provision of technical assistance to, *inter alia*: (a) develop a HDM4-based pavement management system for the Eligible State road network; (b) design a pilot comprehensive maintenance program; (c) develop road transport planning methodologies for the Eligible State; (d) carry out annual Eligible State road condition inventories and update the above-referred HDM4-based pavement management system; (e) coordinate and supervise the execution of Part A of the Project; (f) design and implement environmental and social assessment procedures and relevant mitigation measures for the Eligible State roads program in a manner consistent with the Environmental and Social Regulations and the Environmental and Social Manual; (g) advance the Eligible State's strategy to complete the decentralization of the management of the federal road network in the Eligible State; (h) analyze long-term options for mobilizing resources for, and increasing private sector participation in the road sector of the Eligible State; (i) promote the introduction of new technology for the Eligible State's road rehabilitation and maintenance program; and (j) carry out studies on the Eligible State's roads safety improvement (including, *inter alia*, identification of accident black-spots, development of an accident database, and designing of a strategy to improve road safety).

3. Construction of new state roads except the 181.9 km. between Silao and San Felipe (said 181.9 km. to be financed by the Inter American Development Bank under a different set of norms and procedures).

4. Improvement of bridges and elimination of bottleneck through, *inter alia*, the building of bypasses, separation of road grades, and improvement of unsafe or restricted spots.
5. Construction and improvement of rural roads.

Part B: Water Supply and Sanitation

1. Provision of technical assistance to improve the Eligible State's water resource management including, *inter alia*: (a) improving the measurement of hydrological cycles; (b) improving the planning of the Eligible State's hydrological resources taking into account productive and economic needs of the region; and (c) reducing overexploitation of aquifers and promoting community participation in the management of aquifers.
2. Extension of water and sanitation services to rural and urban communities of the Eligible State.
3. Extension of wastewater treatment facilities to Municipalities of the Eligible State with more than 20,000 inhabitants.
4. Provision of technical assistance to the CEAG to, *inter alia*: (a) train CEAG's staff; (b) certify CEAG's high and medium level managers and CEAG's processes; (c) disseminate educational materials to promote a sustainable water use culture; (d) develop regulatory proposals and practical options to improve CEAG's ability to participate in the setting of appropriate tariffs levels; (e) develop financial mechanisms for the Eligible State's water sector that promote efficiency and establish adequate incentives to achieve sustainable services and adequate service quality; and (f) improve the Eligible State's hydrological and water sanitation services' information system.
5. Strengthen the capacity of water operators in the Eligible State to, *inter alia*, increase their efficiency in the provision of water supply and sanitation services, improve their commercial and technical practices, design adequate tariff structures, improve water awareness among water users (through, *inter alia*, public education campaigns), and carry out supervision of civil work contractors, all of these, through the provision of technical assistance to, *inter alia*: (a) carry out diagnoses on the technical efficiency of systems for controlling water leaks, and on alternative sanitation technologies; (b) improve commercial efficiency and transparency; (c) improve financial sustainability of water operators; and (d) disseminate best practices between water operators.

Part C: Low-Income Housing

1. Provision of technical assistance to strengthen the institutional capacity of the Eligible State and IVEG to, *inter alia*: (a) develop and implement a long term strategy for the housing sector of the Eligible State (including IVEG); (b) define and implement a

subsidy strategy for IVEG's housing programs; (c) carry out seminars to analyze and discuss policy and implementation alternatives for the Eligible State's housing strategy; (d) develop and implement information systems to allow IVEG to link the Eligible State's low income housing programs to the Eligible State's housing development objectives; and (e) develop a framework including environmental and social best practices for the Eligible State's housing sector.

2. (a) Provision of financial assistance to low-income families earning up to four Minimum Mexican wages (Zone C) for housing acquisition through the Eligible State's program *Vivienda Progresiva*, published in the Official Gazette of the Eligible State on February 27, 2004, pages 22 through 25.

(b) Provision of financial assistance to households earning up to three Minimum Mexican wages (Zone C) for housing construction, acquisition or improvement through the Eligible State's programs *Autoconstrucción Institucional*, *Enganches Institucionales* and *Lotes con Servicios*, published in the Official Gazette of the Eligible State on February 27, 2004.

Part D: Institutional Strengthening

1. Provision of technical assistance to strengthen the Eligible State's mechanisms to screen, prioritize and monitor public investments, including the development of methodologies to incorporate systematic economic, financial and social analysis and criteria into evaluation of the Eligible State's investment plans, and the carrying out of multi-sector and multi-annual evaluations of the Eligible State's infrastructure sector activities.

2. Provision of technical assistance and training to strengthen consultation and community participation mechanisms at the Eligible State's state and municipal level.

3. Provision of technical assistance to strengthen the Eligible State's environmental and social policies and practices, including, *inter alia*, the policies and practices of the Ecological Institute of the Eligible State, the Social and Human Development Secretariat of the Eligible State, SOP, IVEG and CEAG.

4. Provision of technical assistance to strengthen the Eligible State's procurement policies and practices, including the carrying out of a standardization of the Eligible State's contracts, the development of offer and ex-post valuation mechanisms, the development of procurement related conflict resolution mechanisms, and the increase of public access to procurement information through *COMPRANET*.

5. Provision of technical assistance to strengthen the Eligible State's financial management systems and processes, including the carrying out of an evaluation of the Eligible State's SAP R/3 platform and processes to determine the Eligible State's

financial management system's requirements and methodologies to assure transparency, good auditing of the Eligible State's public accounts and accountability.

* * *

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

SCHEDULE 3

Amortization Schedule

1. The following table sets forth the Principal Payment Dates of the Loan and the percentage of the total principal amount of the Loan payable on each Principal Payment Date (Installment Share). If the proceeds of the Loan shall have been fully withdrawn as of the first Principal Payment Date, the principal amount of the Loan repayable by the Borrower on each Principal Payment Date shall be determined by the Bank by multiplying: (a) the total principal amount of the Loan withdrawn and outstanding as of the first Principal Payment Date; by (b) the Installment Share for each Principal Payment Date, such repayment amount to be adjusted, as necessary, to deduct any amounts referred to in paragraph 4 of this Schedule, to which a Currency Conversion applies.

<u>Payment Date</u>	<u>Installment Share</u> <u>(Expressed as a %)</u>
On each February 1 and August 1	
Beginning on August 1, 2006 through August 1, 2021	3.13%
On February 1, 2022	2.97%

2. If the proceeds of the Loan shall not have been fully withdrawn as of the first Principal Payment Date, the principal amount of the Loan repayable by the Borrower on each Principal Payment Date shall be determined as follows:

(a) To the extent that any proceeds of the Loan shall have been withdrawn as of the first Principal Payment Date, the Borrower shall repay the amount withdrawn and outstanding as of such date in accordance with paragraph 1 of this Schedule.

(b) Any withdrawal made after the first Principal Payment Date shall be repaid on each Principal Payment Date falling after the date of such withdrawal in amounts determined by the Bank by multiplying the amount of each such withdrawal by a fraction, the numerator of which shall be the original Installment Share specified in the table in paragraph 1 of this Schedule for said Principal Payment Date (the Original Installment Share) and the denominator of which shall be the sum of all remaining Original Installment Shares for Principal Payment Dates falling on or after such date, such repayment amounts to be adjusted, as necessary, to deduct any amounts referred to in paragraph 4 of this Schedule, to which a Currency Conversion applies.

3. (a) Withdrawals made within two calendar months prior to any Principal Payment Date shall, for the purposes solely of calculating the principal amounts payable on any Principal Payment Date, be treated as withdrawn and outstanding on the second Principal Payment Date following the date of withdrawal and shall be repayable on each Principal Payment Date commencing with the second Principal Payment Date following the date of withdrawal.

(b) Notwithstanding the provisions of sub-paragraph (a) of this paragraph 3, if at any time the Bank shall adopt a due date billing system under which invoices are issued on or after the respective Principal Payment Date, the provisions of such sub-paragraph shall no longer apply to any withdrawals made after the adoption of such billing system.

4. Notwithstanding the provisions of paragraphs 1 and 2 of this Schedule, upon a Currency Conversion of all or any portion of the withdrawn principal amount of the Loan to an Approved Currency, the amount so converted in said Approved Currency that shall be repayable on any Principal Payment Date occurring during the Conversion Period, shall be determined by the Bank by multiplying such amount in its currency of denomination immediately prior to said Conversion by either: (i) the exchange rate that reflects the amounts of principal in said Approved Currency payable by the Bank under the Currency Hedge Transaction relating to said Conversion; or (ii) if the Bank so determines in accordance with the Conversion Guidelines, the exchange rate component of the Screen Rate.

5. If the principal amount of the Loan withdrawn and outstanding from time to time shall be denominated in more than one Loan Currency, the provisions of this Schedule shall apply separately to the amount denominated in each Loan Currency, so as to produce a separate amortization schedule for each such amount.

SCHEDULE 4

Procurement

Section I. General

A. All goods, works and services (other than consultants' services) shall be procured in accordance with the provisions of Section I of the "Guidelines for Procurement under IBRD Loans and IDA Credits" dated May 2004 (the Procurement Guidelines), and with the provisions of this Schedule. If the Borrower employs any procurement or inspection agents, it shall ensure that the requirements of Section 3.10 and 3.11 of the Procurement Guidelines are met.

B. All consultants' services shall be procured in accordance with Section I, paragraphs 3.15 through 3.20, and Section IV of, and Appendix 2 to, the "Guidelines: Selection and Employment of Consultants by World Bank Borrowers" dated May 2004 (the Consultant Guidelines), and with the provisions of this Schedule.

Section II. Particular Methods of Procurement of Goods, Works and Services (other than Consultants' Services)

A. International Competitive Bidding. Except as otherwise provided in Part B of this Section, contracts shall be awarded on the basis of international competitive bidding in accordance with the provisions of Section II and paragraphs 3.14 and 3.15 of the Procurement Guidelines, and the following additional procedures:

1. Dispute Review Board. Each contract for works estimated to cost \$50,000,000 equivalent or more shall include the provisions for a dispute review board set forth in the standard bidding documents for works referred to in paragraph 2.43 of the Procurement Guidelines.

2. Grouping of Contracts. To the extent possible, contracts for goods and services (other than consultants' services) shall be grouped in bid packages estimated to cost \$500,000 equivalent or more each and contracts for works shall be grouped in bid packages estimated to cost \$10,000,000 or more.

3. Notification and Advertising

The invitation to bid for each contract shall be advertised in COMPRANET.

B. Other Procurement Procedures

Goods and services (other than consultants' services) estimated to cost less than \$500,000 equivalent per contract and works estimated to cost less than \$10,000,000 equivalent per contract shall be procured in accordance with the Procurement Law, the Procurement Plan and the following provisions:

(a) the procedures referred under Article 26, Section I (*Licitación pública*) of the Guarantor's Procurement of Goods Law shall apply for the procurement of contracts of goods except that contracts for goods estimated to cost less than \$100,000 equivalent per contract may be procured in accordance with the procedures referred under Article 26, Section II (*Invitación a cuando menos tres personas*) of the Guarantor's Procurement of Goods Law;

(b) the procedures referred under Article 27, Section I (*Licitación Pública*) of the Guarantor's Procurement of Works Law shall apply for the procurement of contracts of works except that contracts for works estimated to cost less than \$500,000 equivalent per contract may be procured in accordance with the procedures referred under Article 27, Section II (*Invitación a cuando menos tres personas*) of the Guarantor's Procurement of Works Law; and

(c) the procedures referred under Article 26, Section III (*Adjudicación directa*) of the Guarantor's Procurement of Goods Law and under Article 27, Section III (*Adjudicación directa*) of the Guarantor's Procurement of Works Law may apply only for the procurement of goods and works for which the Bank has authorized the use of said procedures by notice to the Borrower in writing.

Section III. Particular Methods of Procurement of Consultants' Services

A. Quality- and Cost-based Selection.

1. Except as otherwise provided in Part B of this Section, consultants' services shall be procured under contracts awarded on the basis of quality and cost in accordance with the provisions of Section II of the Consultant Guidelines. For purposes of paragraph 2.7 of the Consultant Guidelines, the short list of consultants for services estimated to cost less than \$500,000 equivalent per contract may comprise entirely national consultants.

2. A specific procurement notice shall be published in *United Nations Development Business* to obtain expressions of interest for contracts for consulting services estimated to cost more than \$200,000 equivalent.

B: Other Procedures

1. Least-cost Selection. Services for assignments which the Bank agrees meet the requirements of paragraph 3.6 of the Consultant Guidelines may be procured under contracts awarded on the basis of lowest cost in accordance with the provisions of paragraphs 3.1 and 3.6 of the Consultant Guidelines.

2. Single Source Selection. Services for tasks for which only one firm is qualified or has experience of exceptional worth for the assignment, may, with the Bank's prior agreement, be procured in accordance with the provisions of paragraphs 3.9 through 3.13 of the Consultant Guidelines.

3. Individual Consultants. Services for specialized advisory assignments that meet the requirements set forth in the first sentence of paragraph 5.1 of the Consultant Guidelines may be procured under contracts awarded to individual consultants in accordance with the provisions of paragraphs 5.2 through 5.3 of the Consultant Guidelines. Under the circumstances described in paragraph 5.4 of the Consultant Guidelines, such contracts may be awarded to individual consultants on a sole-source basis in accordance with the provisions of said paragraph 5.4, subject to prior approval of the Bank.

Section IV. Review by the Bank of Procurement Decisions

A. Prior Review. The following review procedures shall apply to contracts for which the Procurement Plan provides for prior review by the Bank:

1. Goods, Works and Services (other than Consultants' Services). The prior review procedures set forth in paragraphs 2, 3 and 4 of Appendix 1 to the Procurement Guidelines shall apply to contracts for goods, works or services (other than consultants' services). However, if such contracts are to be procured on the basis of direct contracting procedures, the following procedures shall apply instead: (a) prior to the execution of such contract, the Borrower shall provide to the Bank a copy of the specifications and the draft contract for its approval; (b) the contract shall be awarded only after the Bank's approval shall have been given; and (c) the procedures set forth in paragraphs 2 (h) and 3 of Appendix 1 to the Guidelines shall apply.

2. Consultants' Services Provided by Firms. The prior review procedures set forth in paragraphs 2, 3 and 4 of Appendix 1 to the Consultant Guidelines shall apply to contracts for consultants' services provided by firms. However, if such contracts are to be procured on the basis of single source selection, the following procedures shall apply instead: (a) the qualifications, experience, terms of reference and conditions of employment of the consultants shall be furnished to the Bank for its prior review and

approval; (b) the contract shall be awarded only after the Bank's approval shall have been given; and (c) the provisions of paragraphs 3 and 5 of Appendix 1 to the Consultant Guidelines shall apply to the contract.

B. Post Review. The following post review procedures shall apply to all contracts for which the Procurement Plan does not provide for prior review by the Bank:

1. With respect to contracts for goods, works or services (other than consultants' services), the post review procedures set forth in paragraph 4 of Appendix 1 to the Procurement Guidelines shall apply.

2. With respect to contracts for consultants' services, the post review procedures set forth in paragraph 4 of Appendix 1 to the Consultant Guidelines shall apply.

SCHEDULE 5

Environmental and Social Regulations

Environmental Assessment	
<p>State of Guanajuato Environmental Protection and Preservation Law (LPPAEG). <i>Ley para Protección y Preservación al Ambiente del Estado de Guanajuato (LPPAEG).</i></p> <p>Published in the Eligible State Official Gazette on February 8, 2000, as amended to the date of this Agreement. http://www.guanajuato.gob.mx/ieeg/n01D_Ley_Proteccion_Prevenccion.htm</p>	<p>Primary state environmental protection and preservation law</p> <p><i>Ley principal del estado de Guanajuato para la protección y preservación del medio ambiente</i></p>
<p>Regulations for State of Guanajuato Environmental Protection and Preservation Law as related to Environmental Impact Assessment <i>Reglamento de la Ley para la Protección y Preservación del Ambiente del Estado de Guanajuato en materia de Evaluación de Impacto Ambiental.</i></p> <p>Published in the Eligible State Official Gazette on September 22, 2000, as amended to the date of this Agreement. http://www.guanajuato.gob.mx/ieeg/n04Reglamento_Ley_MIA.htm</p>	<p>Requirements for conducting Environmental Impact Assessments</p> <p><i>Requisitos para llevar a cabo evaluaciones ambientales</i></p>
<p>Delisting Procedures for Environmental Impact Assessment in Public State and Municipal Works for Guanajuato <i>Proceso de Desregulación en Materia de la Evaluación de Impacto Ambiental de la Obra Pública Estatal y Municipal del Estado de Guanajuato</i></p> <p>Published in the Eligible State Official Gazette on August 21, 2001, as amended to the date of this Agreement. http://www.guanajuato.gob.mx/ieeg/n11Acuerdo_Desregulacion.htm</p>	<p>Minor works are exempted from the normal Environmental Impact Assessment process</p> <p><i>Obras públicas menores están exentas del proceso regular de evaluación ambiental</i></p>
Natural Habitats	
<p>Regulations for State of Guanajuato Environmental Protection and Preservation Law as related to Protected Areas. <i>Reglamento de la Ley para la Protección y Preservación del Ambiente del Estado de Guanajuato en materia de Áreas Naturales Protegidas.</i></p> <p>Published in the Eligible State Official Gazette on September 19, 2000,</p>	<p>Regulations for Creating and Managing Protected Areas</p> <p><i>Reglamentos que rigen la creación y</i></p>

as amended to the date of this Agreement. http://www.guanajuato.gob.mx/ieeg/n03Reglamento Lev MAN.htm	<i>administración de Áreas Naturales Protegidas</i>
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Indigenous Peoples	
<p>National Constitution: Articles 2 and 4. <i>Constitución Política de los Estados Unidos Mexicanos: Artículos 2º y 4º</i></p> <p>Published in the Guarantor’s Official Gazette on February 5, 1917, as amended to the date of this Agreement. http://www.cddhcu.gob.mx/leyinfo/pdf/1.pdf</p>	<p>Protection of cultural diversity and indigenous rights <i>Protección a la diversidad cultural y derechos indígenas</i></p>
<p>National Commission for Indigenous Communities Development Law <i>Ley de la Comisión Nacional para el Desarrollo de los Pueblos Indígenas</i></p> <p>Published in the Guarantor’s Official Gazette on May 21, 2003, as amended to the date of this Agreement. http://cdi.gob.mx/index.php?option=displaypage&Itemid=56&op=page&SubMenu=</p>	<p>Details protection mechanisms <i>Mecanismos de protección específicos</i></p>
<p>Convention 169 of the ILO ratified by México on September 5, 1990 <i>Convenio 169 de la OIT ratificado por México el 5 de septiembre de 1990</i></p> <p>http://www.endepa.org.ar/Convenio169.htm</p>	<p>Protection of indigenous peoples rights <i>Protección al territorio y derechos al trabajo</i></p>
<p>Framework for Federal Public Administration Law, Article 32 (SEDESOL) <i>Ley Orgánica de la Administración Pública Federal Art. 32 (SEDESOL)</i></p> <p>Published in the Guarantor’s Official Gazette on December 29, 1976, as amended to the date of this Agreement. http://www.cddhcu.gob.mx/leyinfo/pdf/153.pdf</p>	<p>Social protection programs for indigenous communities <i>Programas sociales de protección a los pueblos indígena</i></p>
Cultural Property	
<p>Federal Monument and Archeology Law <i>Ley Federal sobre Monumentos y Zonas Arqueológicas, Artísticas e Históricas</i></p> <p>Published in the Guarantor’s Official Gazette on May 6, 1972, as amended to the date of this Agreement. http://www.cddhcu.gob.mx/leyinfo/pdf/131.pdf</p>	<p>Protection of known cultural resources or “chance finds”. <i>Protección a bienes identificados o por encuentros fortuitos</i></p>
<p>Framework Law for National Anthropology and History Institute <i>Ley Orgánica del Instituto Nacional de Antropología e Historia</i></p> <p>Published in the Guarantor’s Official Gazette on February 3, 1939, as amended to the date of this Agreement.</p>	<p>Outlines responsibilities <i>Delimitación de responsabilidades</i></p>

http://www.cddhcu.gob.mx/leyinfo/pdf/170.pdf	
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Involuntary Resettlement	
<p>Agrarian Law <i>Ley Agraria</i></p> <p>Published in the Guarantor's Official Gazette on February 26, 1992, as amended to the date of this Agreement. http://www.cddhcu.gob.mx/leyinfo/pdf/13.pdf</p>	<p>Agricultural, <i>ejido</i>, and communal lands and property. <i>Tierras agrícolas y bienes ejidales y comunales</i></p>
<p>Civil Federal Code <i>Código Civil Federal</i></p> <p>Published in the Guarantor's Official Gazette on May 26, 1928, as amended to the date of this Agreement. http://www.cddhcu.gob.mx/leyinfo/pdf/2.pdf</p>	<p>Private lands and property <i>Tierras y bienes privados</i></p>
<p>Expropriation Law <i>Ley de Expropiación</i></p> <p>Published in the Guarantor's Official Gazette on November 25, 1936 http://www.cddhcu.gob.mx/leyinfo/pdf/35.pdf</p>	<p>Compensation procedures and mechanisms <i>Procedimientos y mecanismos de compensación</i></p>
<p>Framework Law for National Property Appraisal <i>Ley Orgánica de la Comisión de Avalúos y Bienes Nacionales (CABIN)</i></p> <p>Published in the Guarantor's Official Gazette on December 6, 1999, as amended to the date of this Agreement. http://www.cabin.gob.mx/index1.html</p>	<p>Appraisal and compensation for agrarian lands and property <i>Avalúos y compensaciones de tierras y bienes agrarios</i></p>
<p>Federal Housing Law <i>Ley Federal de Vivienda</i></p> <p>Published in the Guarantor's Official Gazette on February 8, 1984, as amended to the date of this Agreement. http://info4.juridicas.unam.mx/ijure/tcfed/125.htm?s=</p>	<p>Regulations to support appropriate human living conditions <i>Reglamentos de apoyo a las condiciones de vida adecuadas para seres humanos</i></p>
<p>General Human Settlement Law <i>Ley General de Asentamientos Humanos</i></p> <p>Published in the Guarantor's Official Gazette on July 21, 1993, as amended to the date of this Agreement. http://www.cddhcu.gob.mx/leyinfo/pdf/133.pdf</p>	<p>Regulations and conditions for human settlements <i>Regulación y condiciones que deben cumplir los asentamientos humanos</i></p>

<p>General Ecological Equilibrium and Environmental Protection Law <i>Ley General del Equilibrio Ecológico y la Protección al Ambiente</i></p> <p>Published in the Guarantor's Official Gazette on January 28, 1988, as amended to the date of this Agreement. http://www.cddhcu.gob.mx/levinfo/pdf/148.pdf</p>	<p>Conditions for new human settlements <i>Condiciones que deben cumplir los nuevos reasentamientos</i></p>
<p>National Constitution: Article 115 <i>Constitución Política de los Estados Unidos Mexicanos Artículo 115</i></p> <p>Published in the Guarantor's Official Gazette on February 5, 1917, as amended to the date of this Agreement. http://www.cddhcu.gob.mx/levinfo/pdf/1.pdf</p>	<p>Municipal responsibilities <i>Responsabilidades de los Municipios</i></p>
<p>State of Guanajuato</p>	
<p>Framework Municipal Law <i>Ley Orgánica Municipal para el Estado de Guanajuato</i></p> <p>Published in the Eligible State's Official Gazette on July 25, 1997, as amended to the date of this Agreement.</p>	<p>Municipal responsibilities for human settlements. <i>Responsabilidades de los municipios sobre asentamientos humanos</i></p>
<p>Subdivision Law <i>Ley de Fraccionamientos</i></p> <p>Published in the Eligible State's Official Gazette on August 15, 2003, as amended to the date of this Agreement.</p>	<p>Land use characteristics for new developments <i>Usos del suelo características de los nuevos desarrollos</i></p>
<p>Disclosure and Access to Information</p>	
<p>Law on Transparency and Access to Information <i>Ley Federal de Transparencia y Acceso a la Información Pública Gubernamental</i></p> <p>Published in the Guarantor's Official Gazette on June 11, 2002, as amended to the date of this Agreement. http://www.cddhcu.gob.mx/levinfo/pdf/244.pdf</p>	<p>Relevant information is public <i>Toda la información contemplada en la Ley es pública</i></p>

SCHEDULE 6

Outputs

	Output	Amount allocated for purposes of Paragraph 2 (c) of Part A of Schedule 1 to this Agreement
1	1 km of road maintained (routine maintenance)	\$1,200
2	1 km of road maintained (periodic maintenance)	\$40,000
3	1 km of road rehabilitated	\$320,000
4	1 km of a rural road improved	\$25,000
5	1 km of annual inventory completed and road condition quantified in terms of roughness	\$290
6	1 additional rural inhabitant with access to water supply services	\$250
7	1 additional rural inhabitant with access to sanitation services	\$250
8	1 additional urban inhabitant connected to water services	\$250
9	1 additional urban inhabitant connected to sanitation services	\$250
10	Each 10% increase in revenue collected per cubic meter of water produced, for water operators that	\$160,000

	serve more than 20,000 inhabitants	
11	1 kg of organic load removed in wastewater plants (measured in modules of 150 kg)	\$400
12	1 loan under the <i>Vivienda Progresiva</i> program to a household earning up to 4 Minimum Mexican wages (Zone C)	\$1,390
13	1 loan under the <i>Lote con Servicios</i> program to a household earning up to 3 Minimum Mexican wages (Zone C)	\$610
14	1 loan under the <i>Autoconstrucción Institucional</i> program to a household earning up to 3 Minimum Mexican wages (Zone C)	\$350
15	1 loan under the <i>Enganches Institucionales</i> program to a household earning up to 3 Minimum Mexican wages (Zone C)	\$350

All outputs will be measured by comparison to the situation in the relevant area as of 12 months prior to the date of this Agreement.