

Public Disclosure Authorized

CONFORMED COPY

CREDIT NUMBER 3834 PAK

Development Credit Agreement

(Second Poverty Alleviation Fund Project)

between

ISLAMIC REPUBLIC OF PAKISTAN

and

INTERNATIONAL DEVELOPMENT ASSOCIATION

Dated January 20, 2004

Public Disclosure Authorized

CREDIT NUMBER 3834 PAK

DEVELOPMENT CREDIT AGREEMENT

AGREEMENT, dated January 20, 2004, between ISLAMIC REPUBLIC OF PAKISTAN acting by its President (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; and

(B) the Project will be carried out by the Pakistan Poverty Alleviation Fund (PPAF) with the Borrower's assistance and, as part of such assistance, the Borrower will make the proceeds of the credit provided for in Article II of this Agreement (the Credit) available to PPAF, as set forth in this Agreement; 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 agreement of even date herewith between the Association and PPAF (the Project Agreement);

NOW THEREFORE the parties hereto hereby agree as follows:

ARTICLE I

General Conditions; Definitions

Section 1.01. The "General Conditions Applicable to Development Credit Agreements" of the Association, dated January 1, 1985 (as amended through October 6, 1999) (the General Conditions), constitute an integral part of this Agreement.

Section 1.02. Unless the context otherwise requires, the several terms defined in the General Conditions and in the Preamble to this Agreement have the respective meanings therein set forth and the following additional terms have the following meanings:

(a) "Beneficiary" means a community organization or group or a village; women's group or committee; mohalla (low income urban neighborhood) group or committee; or self-help organization, group or committee, and includes, for purposes of Sub-loans (as hereinafter defined) only, an individual belonging to any such organization, group or committee;

(b) "Eligible Categories" means Categories (1), (2), (3), (4), (5), (6) and (7) set forth in the table in Part A.1 of Schedule 1 to this Agreement;

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

(d) “Environmental Management Framework” means the environmental management framework dated June 24, 2003, satisfactory to the Association, within which Subprojects shall be implemented, as the same may be amended from time to time with the agreement of the Association;

(e) “EDF” means PPAF’s Enterprise Development Facility as described in the Operations Manual (as hereinafter defined);

(f) “Financial Monitoring Report” or “FMR” means each report prepared in accordance with Section 4.02 of the Project Agreement;

(g) “Fiscal Year” means the Fiscal Year of the Borrower beginning on July 1 of a calendar year and ending on June 30 of the following calendar year;

(h) “Grant” means a grant made or proposed to be made through a PO (as hereinafter defined) out of the proceeds of the Credit to a Beneficiary for an SSIP or SSDP (both as hereinafter defined);

(i) “MCP” means a Micro-Credit Project financed or proposed to be financed under Part A (i) of the Project;

(j) “Memorandum and Articles of Association” means the Memorandum and Articles of Association of PPAF dated January 9, 1997, as the same may be amended from time to time with the agreement of the Association;

(k) “Operations Manual” means PPAF’s comprehensive operations manual dated June 25, 2003, satisfactory to the Association, containing PPAF’s eligibility criteria and appraisal, approval and supervision rules and procedures for POs, Beneficiaries and Subprojects (as hereinafter defined), as the same may be amended from time to time with the agreement of the Association;

(l) “Project Agreement” means the agreement between the Association and PPAF 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;

(m) “PO” or “Partner Organization” means a Non-governmental Organization (NGO), Rural Support Program (RSP), Community Based Organization (CBO) or private sector institution or entity, which is involved in poverty alleviation work, which meets the eligibility criteria for POs set forth in the Operations Manual, and which has made or proposes to make a Sub-loan or Grant;

(n) “PO Financing Agreement” means an agreement to be entered into between PPAF and a PO pursuant to paragraph 3 (c) of Part A of Schedule 2 to the Project Agreement;

(o) “PPAF” means the Pakistan Poverty Alleviation Fund, an autonomous entity registered as a public non-profit company under Section 42 of the Borrower’s Companies Ordinance, 1984 and established as of February 6, 1997;

(p) “Report-based Disbursements” means the Borrower’s option for withdrawal of funds from the Credit Account referred to in Part A.4 of Schedule 1 to this Agreement;

(q) “Rs” or “rupees” means the currency of the Borrower;

(r) “Special Account” means the account referred to in Part B of Schedule 1 to this Agreement;

(s) “SSIP” means a Small-Scale Community Infrastructure Development Project financed or proposed to be financed under Part A (ii) of the Project;

(t) “SSDP” means a Social Sector Development Project financed or proposed to be financed under Part A (iii) of the Project;

(u) “Sub-loan” means a loan made or proposed to be made by a PO out of the proceeds of the Credit to a Beneficiary for an MCP;

(v) “Subproject” means an MCP or SSIP or SSDP depending on the context;

(w) “Subproject Financing Agreement” means an agreement to be entered into between a PO and a Beneficiary, in the case of a Sub-loan, pursuant to paragraph 3(g) of Part B of Schedule 2 to the Project Agreement, or, in the case of a Grant, pursuant to paragraphs 3(g) and 3(h) of Part B of Schedule 2 to the Project Agreement; and

(x) “Subsidiary Financing Agreement” means the agreement to be entered into between the Borrower and PPAF pursuant to Section 3.01(b) of this Agreement, as the same may be amended from time to time, and such term includes all schedules to the Subsidiary Financing 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 one hundred sixty-eight million one hundred thousand Special Drawing Rights (SDR 168,100,000).

Section 2.02. 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 works, goods and services required for Part B of the Project described in Schedule 2 to this Agreement and to be financed out of the proceeds of the Credit; and (ii) amounts paid (or, if the Association shall so agree, amounts to be paid) through PPAF to a PO on account of withdrawals made by a Beneficiary under a Subproject under Part A of the Project to meet the reasonable cost of works, goods and services required for the Subproject and to be financed out of the proceeds of the Credit.

Section 2.03. The Closing Date shall be July 31, 2008, 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 February 1 and August 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 semiannual installments payable on each February 1 and August 1 commencing February 1, 2014 and ending August 1, 2038. Each installment to and including the installment payable on August 1, 2023, shall be one and one-fourth percent ($1-1/4\%$) of such principal amount, and each installment thereafter shall be two and one-half percent ($2-1/2\%$) 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 Association 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.

Section 2.09. The Chief Executive Officer of PPAF, and any person 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, without any limitation or restriction upon any of its other obligations under the Development Credit Agreement, shall cause PPAF to perform in accordance with the provisions of the Project Agreement all the obligations of PPAF 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 PPAF to perform such obligations, and shall not take or permit to be taken any action which would prevent or interfere with such performance.

(b) Without limiting the generality of paragraph (a) of this Section, the Borrower shall:

- (i) make available to PPAF the proceeds of the Credit under a Subsidiary Financing Agreement to be entered into between the Borrower and PPAF, under terms and conditions which shall have been approved by the Association and which shall include the terms and conditions set forth in Schedule 3 to this Agreement; and
- (ii) in accordance with a previous undertaking, in addition, provide to PPAF, from its own resources, an equity contribution in an amount of five hundred million rupees (Rs. 500,000,000) in three installments, payable as follows:
 - (aa) one hundred fifty million rupees (Rs. 150,000,000) at the beginning of FY 2005;
 - (bb) one hundred fifty million rupees (Rs. 150,000,000) at the beginning of FY 2006; and

(cc) two hundred million rupees (Rs. 200,000,000) at the beginning of FY 2007.

(c) The Borrower shall exercise its rights under the Subsidiary Financing 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 Financing Agreement or any provision thereof.

Section 3.02. Except as the Association shall otherwise agree, procurement of the goods, works and consultants' services required for the Project and to be financed out of the proceeds of the Credit shall be governed by the provisions of Schedule 1 to the Project Agreement.

Section 3.03. 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) shall be carried out by PPAF pursuant to Section 2.03 of the Project Agreement.

ARTICLE IV

Financial Covenants

Section 4.01. (a) For all expenditures with respect to which withdrawals from the Credit Account were made on the basis of statements of expenditure or Financial Monitoring Reports, the Borrower shall:

- (i) maintain or cause to be maintained in accordance with sound accounting practices, records and separate accounts reflecting such expenditures;
- (ii) ensure that all records (contracts, orders, invoices, bills, receipts and other documents) evidencing such expenditures are retained until at least one year after the Association has received the audit report for the fiscal year in which the last withdrawal from the Credit Account was made; and
- (iii) enable the Association's representatives to examine such records.

- (b) The Borrower shall:
- (i) have the records and accounts referred to in paragraph (a)(i) of this Section and those for the Special Account for each Fiscal Year audited, in accordance with appropriate auditing principles consistently applied, by independent auditors acceptable to the Association;
 - (ii) furnish to the Association as soon as available, but in any case not later than six months after the end of each such year the report of such audit by said auditors, of such scope and in such detail as the Association shall have reasonably requested, including a separate opinion by said auditors as to whether the Financial Monitoring Reports or statement of expenditures submitted during such fiscal year, together with the procedures and internal controls involved in their preparation, can be relied upon to support the related withdrawals; 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.

Section 4.02. (a) If an event occurs which, in the opinion of the Association, adversely affects or may affect PPAF's equity, the Borrower shall promptly consult with the Association and prepare and thereafter implement a remedial action plan satisfactory to the Association. For the purposes of this provision, PPAF's equity shall be deemed to have been adversely affected if at any time it falls by 10% or more.

(b) For the purposes of this Section, the term "equity" means the sum of payments received for capital purposes including payments to PPAF's endowment fund, retained earnings and free reserves not allocated to cover specific liabilities.

ARTICLE V

Remedies of the Association

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

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

(b) 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 PPAF will be able to perform its obligations under the Project Agreement.

(c) The Memorandum and Articles of Association shall have been amended, suspended, abrogated, repealed or waived so as to affect materially and adversely the ability of PPAF to perform any of its obligations under the Project Agreement.

(d) The Borrower or any other authority having jurisdiction shall have taken any action for the dissolution or disestablishment of PPAF or for the suspension of its operations.

(e) The Borrower shall have taken any action (including the repeal, amendment, suspension, abrogation or waiver of existing legislation and regulations or the introduction of new legislation or regulations) which, in the opinion of the Association, materially or adversely affects the operations or financial condition of POs, or a significant majority of them.

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

(a) the event specified in paragraph (a) of Section 5.01 of this Agreement shall occur and shall continue for a period of 60 days after notice thereof shall have been given by the Association to the Borrower; and

(b) the events specified in paragraphs (c), (d) and (e) of Section 5.01 of this Agreement shall occur.

ARTICLE VI

Effective Date; Termination

Section 6.01. The following event is specified as an additional condition to the effectiveness of the Development Credit Agreement within the meaning of Section 12.01(b) of the General Conditions, namely, that the Subsidiary Financing Agreement has been executed on behalf of the Borrower and PPAF.

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 PPAF, and is legally binding upon PPAF in accordance with its terms; and

(b) that the Subsidiary Financing Agreement has been duly authorized or ratified by the Borrower and PPAF and is legally binding upon the Borrower and PPAF 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. Except as provided in Section 2.09 of this Agreement, the Secretary to the Government of Pakistan, Economic Affairs Division, or any Additional Secretary, Joint Secretary, Deputy Secretary or Section Officer in the Economic Affairs Division 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:

The Secretary to the Government of Pakistan
Economic Affairs Division
Islamabad
Pakistan

Cable address:	Telex:	Facsimile:
ECONOMIC Islamabad	ECDIV-05-634	92 51 9205971 92 51 9210734

For the Association:

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

Cable address:	Telex:	Facsimile:
INDEVAS 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 Islamabad, Pakistan, as of the day and year first above written.

ISLAMIC REPUBLIC OF PAKISTAN

By /s/ Waqar Masood Khan

Authorized Representative

INTERNATIONAL DEVELOPMENT ASSOCIATION

By /s/ Abid Hasan

Acting Country Director
Pakistan

SCHEDULE 1

Withdrawal of the Proceeds of the Credit

A. General

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

<u>Category</u>	<u>Amount of the Credit Allocated (Expressed in SDR Equivalent)</u>	<u>% of Expenditures to be Financed</u>
(1) Sub-loans provided:		100% of amounts disbursed by PPAF
(a) other than through EDF	92,670,000	
(b) through EDF	1,470,000	
(2) Grants for:		100% of amounts disbursed by PPAF
(a) SSIPs	39,390,000	
(b) SSDPs	3,530,000	
(3) Civil works	1,260,000	90%
(4) Equipment and vehicles for:		100% of foreign expenditures, 100% of local expenditures (ex-factory cost) and 70% of local expenditures for other items procured locally
(a) PPAF	490,000	
(b) POs	3,460,000	
(5) Consultants' and external auditors' services for PPAF	2,340,000	88% of expenditures for foreign firms or individuals and 98% of expenditures for local firms or individuals

<u>Category</u>	<u>Amount of the Credit Allocated (Expressed in SDR Equivalent)</u>	<u>% of Expenditures to be Financed</u>
(6) Training for:		100%
(a) PPAF	490,000	
(b) POs	1,910,000	
(c) Beneficiaries	3,960,000	
(7) Incremental Operating Costs for:		
(a) PPAF	1,450,000	65% of expenditures for Year 1 of the Project, 55% of expenditures for Year 2 of the Project, 45% of expenditures for Year 3 of the Project, and 0% of expenditures for Year 4 of the Project
(b) POs	14,270,000	100% of amounts disbursed by PPAF to finance, on a declining basis, such percentage of each PO's operating costs as shall be determined by PPAF, based on the PO's business plan
(8) Unallocated	1,410,000	
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TOTAL	168,100,000	
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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;

(c) the term “foreign firms or individuals” means firms that are registered or incorporated in the territory, or, as the case may be, individuals who are nationals, of any country other than that of the Borrower;

(d) the term “local firms or individuals” means firms that are registered or incorporated in the territory, or, as the case may be, individuals who are nationals, of the Borrower; and

(e) the term “incremental operating costs” means:

(i) in respect of PPAF, salaries, per diem, and fringe benefits of staff appointed to posts in PPAF on or after July 1, 2003, and engaged on a full-time basis for the purposes of the Project, including conveyance, travel and boarding/lodging allowances when on tour, and operating and maintenance costs of vehicles, equipment and offices acquired under and used in the carrying out of the Project, including the costs of advertising, media projections, newspaper subscriptions, periodicals, insurance, printing, stationary, rent and utilities; and

(ii) in respect of a PO, the salaries, allowances and other emoluments of staff of the PO appointed to posts created after the signing of the relevant PO Financing Agreement and engaged on a full-time basis for the purposes of the Project, including conveyance, travel and boarding/lodging allowances when on tour, and operating and maintenance costs of vehicles, equipment and offices acquired under and used in the carrying out of the Project, including the costs of advertising, media projections, newspaper subscriptions, periodicals, insurance, printing, stationary, rent and utilities.

3. Notwithstanding the provisions of paragraph 1 above, no withdrawals shall be made in respect of payments made for expenditures prior to the date of this Agreement, except that withdrawals in an aggregate amount not exceeding the equivalent of \$10,000,000 may be made in respect of Categories (1), (2), (3), (4), (5), (6) and (7) on account of payments made for expenditures before that date but after July 1, 2003.

4. The Association may require withdrawals from the Credit Account to be made on the basis of statements of expenditure for expenditures: (a) for all Sub-loans, Grants, training, audit costs and incremental operating costs; (b) under contracts for equipment and vehicles, and works costing less than \$200,000 equivalent per contract; (c) under contracts for services of consulting firms under contracts costing less than \$100,000

equivalent per contract; and (d) under contracts for services of individual consultants costing less than \$50,000 equivalent per contract, all under such terms and conditions as the Association shall specify by notice to the Borrower.

5. The Borrower may request withdrawals from the Credit Account to be made on the basis of reports to be submitted to the Association in form and substance satisfactory to the Association, such reports to include the FMR and any other information as the Association shall specify by notice to the Borrower (Report-based Disbursements). In the case of the first such request submitted to the Association before any withdrawal has been made from the Credit Account, the Borrower shall submit to the Association 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 may open and maintain in Dollars a special deposit account in a commercial bank acceptable to the Association, on terms and conditions satisfactory to the Association, including appropriate protection against set-off, seizure and attachment.

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

(a) 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 Association shall reasonably request, furnish to the Association such documents and other evidence showing that such payment was made exclusively for Eligible Expenditures.

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

(a) if the Association, 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 Association determines at any time that all further withdrawals for payment of Eligible Expenditures should be made by the Borrower directly from the Credit Account; or

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

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

6. (a) If the Association determines at any time that any payment out of the Special Account was made for an expenditure which is not an Eligible Expenditure, or was not justified by the evidence furnished to the Association, the Borrower shall, promptly upon notice from the Association, provide such additional evidence as the Association may request, or deposit into the Special Account (or, if the Association shall so request, refund to the Association) an amount equal to the amount of such payment. Unless the Association shall otherwise agree, no further deposit by the Association into the Special Account shall be made until the Borrower has provided such evidence or made such deposit or refund, as the case may be.

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

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

(d) Refunds to the Association made pursuant to subparagraph (a), (b) or (c) of this paragraph 6 shall be credited to the Credit Account for subsequent withdrawal or for cancellation in accordance with the provisions of 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 \$20,000,000 to be withdrawn from the Credit Account and deposited into the Special Account pursuant to paragraph 2 of this Annex.

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

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

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

3. The Association shall not be required to make further deposits into the Special Account, once the total unwithdrawn amount of the Loan minus the total amount of all outstanding special commitments entered into by the Association pursuant to Section 5.02 of the General Conditions shall equal the equivalent of twice the amount of the Authorized Allocation. Thereafter, withdrawal from the Credit Account of the remaining unwithdrawn amount of the Loan shall follow such procedures as the Association shall specify by notice to the Borrower. Such further withdrawals shall be made only after and to the extent that the Association shall have been satisfied that all such amounts remaining on deposit in the Special Account as of the date of such notice will be utilized in making payments for Eligible Expenditures.

**Annex B
to
SCHEDULE 1**

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

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

2. Upon receipt of each application for withdrawal of an amount of the Credit, the Association shall, on behalf of the Borrower, withdraw from the Credit Account and deposit into the Special Account an amount equal to the lesser of: (a) the amount so requested; and (b) the amount which the Association has determined, based on the 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.

SCHEDULE 2

Description of the Project

The objective of the Project is to alleviate poverty by improving the access of the rural and urban poor to economic resources and services.

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: Subprojects

Financing of:

- (i) micro-credit projects to support income generating activities;
- (ii) small-scale community infrastructure development projects to support the development, construction, upgrading and improvement of infrastructure; and
- (iii) social sector development projects to support the provision of education and/or health services.

Part B: Institutional Capacity Building

1. Strengthening of the operational capacity of PPAF, through the provision of office buildings, equipment and vehicles, technical assistance for improving information management and financial systems and for carrying out studies, training, and financing for incremental operating costs; and
2. Strengthening of the operational capacity of POs, through the provision of equipment and vehicles, technical assistance for improving information management and financial systems, training in implementing poverty alleviation programs, with emphasis on community mobilization and participatory approaches, and financing for incremental operating costs.

* * *

The Project is expected to be completed by January 31, 2008.

SCHEDULE 3

Financing Terms and Conditions Referred to in Section 3.01(b)(i) of this Agreement

1. Except as the Association shall otherwise agree:
 - (a) with respect to amounts of the Credit allocated from time to time to Category (1) of the table set forth in Part A.1 of Schedule 1 to this Agreement for the purposes of making Sub-loans, PPAF shall:
 - (i) pay to the Borrower, interest at the rate of three-fourths of one percent ($\frac{3}{4}$ of 1%) per annum on the principal amount of the Credit withdrawn by PPAF and outstanding from time to time;
 - (ii) pay to the Borrower, a commitment charge on the principal amount of the Credit not withdrawn by PPAF from time to time at a rate equal to the rate for the time being set by the Association pursuant to Section 2.04 (a) of this Agreement;
 - (iii) repay to the Borrower, the principal amount of the Credit withdrawn by PPAF over a period of 23 years including a grace period of 8 years, such principal amount being the aggregate equivalent of the amounts withdrawn by PPAF from the Credit Account expressed in rupees determined as of the respective dates of withdrawal; and
 - (b) amounts of the Credit allocated, from time to time, to Category (2) of the table set forth in Part A.1 of Schedule 1 to this Agreement for the purposes of making Grants and to Categories (3), (4), (5), (6) and (7) of said table shall be made available to PPAF on a non-reimbursable basis.
2. Except as the Association shall otherwise agree, the Borrower shall suspend or terminate PPAF's right to use the proceeds of the Credit:
 - (a) upon failure by PPAF to perform any of its obligations under the Subsidiary Financing Agreement; or
 - (b) upon notice by the Association to the Borrower that it intends to exercise any of its remedies under Sections 6.02 and 7.01 of the General Conditions or Article V of this Agreement; or
 - (c) upon notice by PPAF that it intends to terminate the Subsidiary Financing Agreement, whichever occurs first.

