

Public Disclosure Authorized

CONFORMED COPY

CREDIT NUMBER 4351-MOT

Financing Agreement

(Energy Community of South East Europe APL 3 – Montenegro Project)

between

THE REPUBLIC OF MONTENEGRO

and

INTERNATIONAL DEVELOPMENT ASSOCIATION

Dated August 28, 2007

CREDIT NUMBER 4351-MOT

FINANCING AGREEMENT

AGREEMENT dated August 28, 2007, between THE REPUBLIC OF MONTENEGRO (“Recipient”) and INTERNATIONAL DEVELOPMENT ASSOCIATION (“Association”). The Recipient and the Association hereby agree as follows:

ARTICLE I - GENERAL CONDITIONS; DEFINITIONS

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

ARTICLE II - FINANCING

- 2.01. The Association agrees to extend to the Recipient, on the terms and conditions set forth or referred to in this Agreement, a credit in an amount equivalent to six million Special Drawing Rights (SDR 6,000,000) (“Credit”) to assist in financing the project described in Schedule 1 to this Agreement (“Project”).
- 2.02. The Recipient may withdraw the proceeds of the Financing in accordance with Section IV of Schedule 2 to this Agreement.
- 2.03. The Maximum Commitment Charge Rate payable by the Recipient on the Unwithdrawn Financing Balance shall be one-half of one percent (1/2 of 1%) per annum.
- 2.04. The Service Charge payable by the Recipient on the Withdrawn Credit Balance shall be equal to three-fourths of one percent (3/4 of 1%) per annum.
- 2.05. The Payment Dates are May 15 and November 15 in each year.
- 2.06. The principal amount of the Credit shall be repaid in accordance with repayment schedule set forth in Schedule 3 to this Agreement.
- 2.07. The Payment Currency is Euro.

ARTICLE III - PROJECT

- 3.01. The Recipient declares its commitment to the objectives of the Project. To this end, the Recipient shall ensure that the EPCG shall carry out the Project in accordance with the provisions of Article IV of the General Conditions.
- 3.02. Without limitation upon the provisions of Section 3.01 of this Agreement, and except as the Recipient and the Association shall otherwise agree, the Recipient shall ensure that the Project is carried out in accordance with the provisions of Schedule 2 to this Agreement.

ARTICLE IV - REMEDIES OF THE ASSOCIATION

- 4.01. The Additional Events of Suspension consist of the following:
 - (a) The EPCG Legislation has been amended, suspended, abrogated, repealed or waived so as to affect materially and adversely the ability of the EPCG to perform any of its obligations under the EPCG Sub-credit Agreement;
 - (b) the Recipient or the EPCG have failed to perform any of their respective obligations under the EPCG Sub-credit Agreement.
- 4.02. The Additional Event of Acceleration consist of the following: any event specified in Section 4.01 of this Agreement occurs and is continuing for a period of sixty (60) days after notice of the event has been given by the Association to the Recipient.

ARTICLE V - EFFECTIVENESS

- 5.01. The Additional Conditions of Effectiveness consist of the following, namely the EPCG Sub-credit Agreement has been signed and all conditions to the effectiveness of such agreement have been fulfilled.
- 5.02. The Additional Legal Matters consist of the following, namely, the EPCG Sub-credit Agreement has been duly authorized by the Recipient and EPCG, and is legally binding upon the Recipient and EPCG in accordance with its terms.
- 5.03. The Effectiveness Deadline is the date ninety (90) days after the date of this Agreement.

ARTICLE VI - REPRESENTATIVE; ADDRESSES

6.01. The Recipient's Representative is the Minister of Finance.

6.02. The Recipient's Address is:

Ministry of Finance
Stanka Dragojevicica 2
81000 Podgorica
Republic of Montenegro

Facsimile:

+382 81 224 450

6.03. The Association's Address is:

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

Cable:

Telex:

Facsimile:

INDEVAS
Washington, D.C.

248423 (MCI) or
64145 (MCI)

1-202-477-6391

AGREED at Podgorica, Republic of Montenegro, as of the day and year first above written.

REPUBLIC OF MONTENEGRO

By /s/ Igor Luksic

Authorized Representative

INTERNATIONAL DEVELOPMENT ASSOCIATION

By /s/ Jan-Peter Olters

Authorized Representative

SCHEDULE 1

Project Description

The objective of the Project is to improve the efficiency and reliability of the power system in the Republic of Montenegro, through better supply security and closer integration into the regional markets.

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

Component 1. Telecommunications System Development

Development of a modern telecommunications network, including links with regional utilities.

Component 2. Transmission Network Reinforcement

Construction of two transmission line circuits from the transmission network to the Andrijevica substation and to the Mojkovac substation.

Component 3. Improvement of Operational Reliability of Perucica Hydropower Plant

Installation of a new trash rack and new trash rack cleaning equipment, and supply of spare turbine runners for Perucica Hydropower Plant.

SCHEDULE 2

Project Execution

Section I. Subsidiary Financing; Institutional and Other Arrangements

A. Subsidiary Agreement

1. To facilitate the carrying out of the Project, the Recipient shall make the proceeds of the Financing available to the EPCG under a subsidiary agreement (“EPCG Sub-credit Agreement”), all under terms and conditions approved by the Association.
2. The Recipient shall exercise its rights under the EPCG Sub-credit Agreement in such manner as to protect the interests of the Recipient and the Association, and to accomplish the purposes of the Financing. Except as the Association shall otherwise agree, the Recipient shall not assign, amend, abrogate or waive the EPCG Sub-credit Agreement of any of its provisions, and shall ensure that the EPCG does not assign, amend, abrogate or waive the EPCG Sub-credit Agreement of any of its provisions.

B. Institutional and Other Arrangements

1. The Recipient shall ensure that the EPCG maintains at all times during the Project implementation a Project management unit, with terms of reference, resources and staff necessary for Project implementation and satisfactory to the Association.
2. The Recipient shall ensure that the EPCG shall implement the Project in accordance with the EMP and LAPF, and shall not assign, amend, abrogate or waive the EMP or the LAPF without the prior approval of the Association.

Section II. Project Monitoring, Reporting, Evaluation

A. Project Reports

1. The Recipient shall ensure that the EPCG monitors and evaluates the progress of the Project and prepares Project Reports in accordance with the provisions of Section 4.08 of the General Conditions and on the basis of indicators agreed with the Association. Each Project Report shall cover the period of one (1) calendar quarter, and shall be furnished to the Association not later than forty five (45) days after the end of the period covered by such report.
2. For purposes of Section 4.08 (c) of the General Conditions, the report on the execution of the Project and related plan required pursuant to that Section shall be furnished to the Association not later than September 30, 2011.

B. Financial Management, Financial Reports and Audits

1. The Recipient shall ensure that the EPCG shall maintain or cause to be maintained a financial management system in accordance with the provisions of Section 4.09 of the General Conditions.
2. Without limitations on the provisions of Part A of this Section, the Recipient shall ensure that the EPCG shall prepare and furnish to the Association as part of the Project Report not later than forty five (45) days after the end of each calendar quarter, interim un-audited financial reports for the Project covering the quarter, in form and substance satisfactory to the Association.
3. The Recipient shall ensure that the EPCG shall have its and Project Financial Statements audited in accordance with the provisions of Section 4.09 (b) of the General Conditions. Each audit of the Financial Statements shall cover the period of one (1) fiscal year of the EPCG. Both the EPCG and the Project audited Financial Statements for each such period shall be furnished to the Association not later than six (6) months after the end of such period.

Section III. Procurement

A. General

1. **Goods.** All goods and services (other than consultants' services) required for the Project and to be financed out of the proceeds of the Financing shall be procured in accordance with the requirements set forth or referred to in Section I of the Procurement Guidelines, and with the provisions of this Schedule.
2. **Definitions.** The capitalized terms used below in this Section to describe particular procurement methods or methods of review by the Association of particular contracts, refer to the corresponding method described in the Procurement Guidelines.

B. Particular Methods of Procurement of Goods

International Competitive Bidding. Goods and services (other than consultants' services) shall be procured under contracts awarded on the basis of International Competitive Bidding.

C. Review by the Association of Procurement Decisions

1. The Procurement Plan shall set forth those contracts which shall be subject to the Association's Prior Review.

2. Except as the Association shall otherwise determine by notice to the Recipient, each contract for goods procured on the basis of International Competitive Bidding shall be subject to Prior Review by the Association.

Section IV. Withdrawal of the Proceeds of the Financing

A. General

1. The Recipient may withdraw the proceeds of the Financing in accordance with the provisions of this Section and such additional instructions as the Association may specify by notice to the Recipient, to finance Eligible Expenditures as set forth in the table in paragraph 2 below.

2. The following table specifies the categories of Eligible Expenditures that may be financed out of the proceeds of the Financing (“Category”), the allocations of the amounts of the Financing to each Category, and the percentage of expenditures to be financed for Eligible Expenditures in each Category:

Category	Amount of the Financing Allocated (expressed in SDR)	Percentage of Expenditures to be Financed
(1) Goods and Services for Component 1	4,000,000	80%
(2) Goods for Components 2 and 3	2,000,000	80%
TOTAL AMOUNT	<u>6,000,000</u>	

B. Withdrawal Conditions; Withdrawal Period

1. Notwithstanding the provisions of Part A of this Section no withdrawal shall be made:
 - (a) for payments made prior to the date of this Agreement; or
 - (b) payment made for expenditures under Category (1) until the EPCG has (i) engaged a consultant under terms of reference and with qualifications satisfactory to the Association, to prepare the design, technical specifications and bidding documents for the activities under Component 1 of the Project; and (ii) adopted a design and technical implementation plan for Component 1 satisfactory to the Association.
2. The Closing Date is March 31, 2012.

Section V. Other Undertakings

A. Self-financing Ratio

The Recipient shall ensure that by January 1, 2008, the EPCG shall maintain a self-financing ratio equal to or above thirty five (35) percent. For the purposes of this Section V.A, the term “self-financing ratio” shall mean the ratio between the funds from internal cash generation and capital expenditures incurred by the EPCG during the calendar year, and the term “funds from internal cash generation” shall mean the difference between: (A) the sum of gross revenues from all sources related to the EPCG’s operations, net non-operating income and any reduction in non-cash working capital; and (B) the sum of all expenses of the EPCG’s operations, including maintenance and administration (excluding depreciation and other non-cash operating charges), interest and other charges on debt, repayment of loans, all taxes or payments in lieu of taxes, all cash dividends and other cash distributions of surplus, increase in non-cash working capital and any other cash outflows other than cash expenditures related to the operations of the EPCG.

B. Collection Ratio

The Recipient shall ensure that that from the start of Project implementation until January 1, 2008, the EPCG shall maintain a collection ratio equal to or above ninety (90) percent, from January 1, 2008 until January 1, 2009, a collection ratio equal to or above ninety two (92) percent, and from January 1, 2009, a collection ratio equal to or above ninety four (94) percent. For the purposes of this Section V.B, the term “collection ratio” shall mean the ratio between the EPCG proceeds of collections from customers during the calendar year and the amount billed to customers during the calendar year for regulated electricity services.

SCHEDULE 3

Repayment Schedule

Date Payment Due	Principal Amount of the Credit repayable (expressed as a percentage)*
On each May 15 and November 15:	
commencing November 15, 2017 to and including May 15, 2027	5%

* The percentages represent the percentage of the principal amount of the Credit to be repaid, except as the Association may otherwise specify pursuant to Section 3.03 (b) of the General Conditions.

APPENDIX

Definitions

1. “Category” means a category set forth in the table in Section IV of Schedule 2 to this Agreement.
2. “EMP” means the Environmental Management Plan adopted by the EPCG on March 31, 2006, and describing the environmental mitigation, monitoring and institutional measures to be undertaken by the EPCG during the implementation of the Project, satisfactory to the Association, as such plan may be amended from time to time with prior agreement of the Association.
3. “EPCG” means “Elektroprivreda Crne Gore Ad-Niksic”, a joint stock company of the Republic of Montenegro responsible for power generation, transmission and distribution in the Republic of Montenegro, registered by the Commercial Court of the Republic of Montenegro on June 15, 1999, or any successor or successors thereto.
4. “EPCG Legislation” means the charter and founding documents establishing the EPCG and governing its operation.
5. “EPCG Sub-credit Agreement” means the agreement referred to in Section I.A.1 of Schedule 2 to this Agreement pursuant to which the Republic of Montenegro shall make the proceeds of the Financing available to the EPCG, as such agreement may be amended from time to time with prior agreement of the Association.
6. “General Conditions” means the “International Development Association General Conditions for Credits and Grants”, dated July 1, 2005.
7. “LAPF” means the Land Acquisition Policy Framework adopted by the EPCG on March 31, 2006, and describing the land acquisition policies and procedures to be adhered to by the EPCG during the implementation of the Project, satisfactory to the Association, as such framework may be amended from time to time with prior agreement of the Association.
8. “Procurement Guidelines” means the “Guidelines for Procurement under IBRD Loans and IDA Credits” published by the Bank in May 2004.
9. “Procurement Plan” means the Recipient’s procurement plan for the Project, dated May 23, 2007, and referred to in paragraph 1.16 of the Procurement Guidelines, as the same shall be updated from time to time in accordance with the provisions of said paragraphs.

