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CONFORMED COPY

GRANT NUMBER H258 -NEP

Financing Agreement

(Additional Financing for Poverty Alleviation Fund Project)

between

NEPAL

and

INTERNATIONAL DEVELOPMENT ASSOCIATION

Dated March 9, 2007

GRANT NUMBER H258-NEP

FINANCING AGREEMENT

AGREEMENT, dated March 9, 2007, between NEPAL (“Recipient”) and INTERNATIONAL DEVELOPMENT ASSOCIATION (“Association”) for the purpose of providing additional financing for activities related to the Original Project (as defined in the Appendix to this Agreement). 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 this 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 grant in an amount equivalent to sixteen million nine hundred thousand Special Drawing Rights (SDR 16,900,000) (“Grant”) 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 Payment Dates are June 15 and December 15 in each year.
- 2.05. The Payment Currency is Dollars.

ARTICLE III – PROJECT

- 3.01. The Recipient declares its commitment to the objectives of the Project. To this end, the Recipient shall cause the Project to be carried out by the Project Implementing Entity in accordance with the provisions of Article IV of the General Conditions and the Project Agreement.

- 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 and Schedule 1 to the Project Agreement.

ARTICLE IV – REMEDIES OF THE ASSOCIATION

- 4.01. The Additional Event of Suspension consists of the following:
- (a) The Project Implementing Entity's Legislation has been amended, suspended, abrogated, repealed or waived so as to affect materially and adversely the ability of the Project Implementing Entity to perform any of its obligations under the Project Agreement.

ARTICLE V – EFFECTIVENESS; TERMINATION

- 5.01. The Additional Conditions of Effectiveness consist of the following:
- (a) The Subsidiary Grant Agreement has been executed on behalf of the Recipient and the Project Implementing Entity.
 - (b) The Project Implementing Entity has prepared the Operational Manual and the Financial Management Manual in form and substance satisfactory to the Association.
- 5.02. The Additional Legal Matter consists of the following:
- (a) The Subsidiary Grant Agreement has been duly authorized or ratified by the Recipient and the Project Implementing Entity and is legally binding upon the Recipient and the Project Implementing Entity in accordance with its terms.
- 5.03. The Effectiveness Deadline is the date ninety (90) days after the date of this Agreement.
- 5.04. For purposes of Section 8.05(b) of the General Conditions, the date on which the provisions of this Agreement shall terminate is twenty (20) years after the date of this Agreement.

ARTICLE VI – REPRESENTATIVE; ADDRESSES

- 6.01. The Recipient's Representative is the Secretary, Ministry of Finance.

6.02. The Recipient's Address is:

Ministry of Finance
Government of Nepal
Singha Durbar
Kathmandu
Nepal

Facsimile:

(977-1) 4259-891

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 Kathmandu, Nepal, as of the day and year first above written.

NEPAL

By /s/ Vidyadhar Mallik

Authorized Representative

INTERNATIONAL DEVELOPMENT ASSOCIATION

By / s/ Kenichi Ohashi

Country Director
Nepal

SCHEDULE 1

Project Description

The objective of the Project is to carry out demand- and community-driven approach to improve access to income-generating Sub-Projects and community infrastructure, benefiting groups excluded by reasons of gender, ethnicity and caste, as well as the poorest groups in rural communities.

The Project consists of the following parts:

Part A: Income Generating Sub-Projects

Provision of Block Grants to Beneficiaries to carry out IGSP in the areas, *inter alia*, of: (i) micro-irrigation; (ii) micro-enterprises; (iii) crafts; (iv) land productivity; and (v) animal husbandry.

Part B: Small-Scale Village and Community Infrastructure Projects (SSIP)

Provision of Block Grants to Beneficiaries to carry out SSIPs in the areas, *inter alia*, of: (i) engineered trails; (ii) footbridges; (iii) schools; and (iv) clinics.

Part C: Innovation and Special Programs

Provision of demand-driven Innovative Grants to selected Beneficiaries for the carrying out of:

- (i) Sub-Projects requiring innovative approaches for targeting and improving livelihoods; and
- (ii) Special Sub-Projects proposed by Beneficiaries.

Part D: Capacity Building and Implementation Support

1. Mobilization of Community Groups

- (i) Carrying out social mobilization activities through POs, to create an enabling environment among Beneficiary groups for the development of funding proposals; and
- (ii) Provision of consultants' services to build the capacity of the POs, and assist them in monitoring implementation of Sub-Projects.

2. Capacity Building for Local Bodies

Provision of consultants' services to build the capacity of selected VDCs and DDCs, and assist them in implementing Sub-Projects.

3. Capacity Building of Beneficiaries

Provision of consultants' services to build the Beneficiaries' capacity in areas including: (i) training of village health workers; (ii) veterinary skills; (iii) crafts skills; (iv) introduction of improved varieties of agricultural produce; (v) marketing; (vi) entrepreneurship; and (vii) bookkeeping.

4. Support to Micro-finance Intermediaries

Provision of consultants' services, on a demand basis, to build the capacity of micro-finance intermediaries.

5. Monitoring and Evaluation System

Provision of consultants' services to monitor, supervise and evaluate the implementation of the Project.

Part E: Administration of the PAF

Strengthening the operational capacity of PAF through the provision of equipment, vehicles, studies and training and technical assistance to improve information management, financial systems, procurement and environmental management.

SCHEDULE 2

Project Execution

Section I. Subsidiary Grant Agreement; Institutional and Other Arrangements

A. Subsidiary Grant Agreement

1. To facilitate the carrying out of the Project by the Project Implementing Entity, the Recipient shall make the proceeds of the Financing available to the Project Implementing Entity under an amendment, with terms and conditions approved by the Association, to the subsidiary grant agreement entered into between the Recipient and the Project Implementing Entity under the Original Project (as so amended, "Subsidiary Grant Agreement").
2. The Recipient shall exercise its rights under the Subsidiary Grant 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 Subsidiary Grant Agreement or any of its provisions.

B. VCDP

The Recipient shall maintain, in form and substance satisfactory to the Association, the VCDP, and implement it in accordance with the objectives, policies, procedures, time schedules and other provisions set forth therein, to ensure that vulnerable people in the Project Area shall benefit fully from the activities financed under the Project.

Section II. Project Monitoring, Reporting, Evaluation

A. Project Reports

The Recipient shall monitor and evaluate the progress of the Project and cause Project Reports to be prepared in accordance with the provisions of Section 4.08 of the General Conditions and on the basis of the indicators set forth in Schedule 3 to the Project Agreement. Each Project Report shall cover the period of a Fiscal Year trimester, and shall be furnished to the Association not later than forty-five (45) days after the end of the period covered by such report.

B. Financial Management, Financial Reports and Audits

1. The Recipient 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 limitation on the provisions of Part A of this Section, the Recipient shall cause to be prepared and furnished to the Association as part of the Project Report not later than forty-five (45) days after the end of each Fiscal Year trimester, interim un-audited financial reports for the Project covering the Fiscal Year trimester, in form and substance satisfactory to the Association.
3. The Recipient shall have its 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 Fiscal Year of the Recipient. The 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 and Works.** All goods and works 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. **Consultants' Services.** All 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 Sections I and IV of the Consultant Guidelines, and with the provisions of this Schedule.
3. **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, or Consultant Guidelines, as the case may be.

B. Particular Methods of Procurement of Goods and Works

1. **National Competitive Bidding.** Except as otherwise provided in paragraph 2 below, goods and works shall be procured under contracts awarded on the basis of National Competitive Bidding, subject to the following additional procedures:
 - (i) Bid opening at only one place and immediately after the deadline of bid submission shall be mandatory;
 - (ii) Local institutions where the Recipient has fifty percent (50%) or more of the capital shall not be exempt from submission of bid and performance securities;

- (iii) Local bidders shall not be eligible for any preference when competing with foreign bidders;
- (iv) Bidders' qualification criteria shall be formulated in accordance with the Bank's Standard Bidding Documents; and
- (v) There shall be no restrictions for foreign bidders to participate in National Competitive Bidding procedures.

2. **Other Methods of Procurement of Goods and Works.** The following table specifies the methods of procurement, other than National Competitive Bidding, which may be used for goods and works. The Procurement Plan shall specify the circumstances under which such methods may be used.

Procurement Method
(a) Shopping
(b) Direct Contracting
(c) Community Participation procedures acceptable to the Association

C. **Particular Methods of Procurement of Consultants' Services**

1. **Quality- and Cost-based Selection.** Except as otherwise provided in paragraph 2 below, consultants' services shall be procured under contracts awarded on the basis of Quality and Cost-based Selection.

2. **Other Methods of Procurement of Consultants' Services.** The following table specifies methods of procurement, other than Quality and Cost-based Selection, which may be used for consultants' services. The Procurement Plan shall specify the circumstances under which such methods may be used.

Procurement Method
(a) Quality-Based Selection
(b) Selection under a Fixed Budget
(c) Least-Cost Selection
(d) Selection Based on Consultants' Qualifications

Procurement Method
(e) Single-Source Selection
(f) Procedures set forth in paragraphs 5.2 and 5.3 of the Consultant Guidelines for the Selection of Individual Consultants
(g) Sole Source Procedures for the Selection of Individual Consultants

D. Review by the Association of Procurement Decisions

The Procurement Plan shall set forth those contracts which shall be subject to the Association’s Prior Review. All other contracts shall be subject to Post 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 Article II of the General Conditions, this Section and such additional instructions as the Association may specify by notice to the Recipient (including the “World Bank Disbursement Guidelines for Projects” dated May 2006, as revised from time to time by the Association and as made applicable to this Agreement pursuant to such instructions), 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) Block Grants for:		100% of amounts disbursed
(a) IGSPs	8,280,000	
(b) SSIPs	5,300,000	
(c) Innovative Grants	450,000	

Category	Amount of the Financing Allocated (Expressed in SDR)	Percentage of Expenditures to be Financed
(2) Consultants' services	1,550,000	100%
(3) Equipment and vehicles for PAF	90,000	100%
(4) Training and knowledge sharing	680,000	100%
(5) Incremental Operating Costs	550,000	80%
TOTAL AMOUNT	16,900,000	

B. Withdrawal Conditions; Withdrawal Period

1. Notwithstanding the provisions of Part A of this Section, no withdrawal shall be made for payments made prior to the date of this Agreement, except that withdrawals up to an aggregate amount not to exceed \$2,000,000 equivalent may be made for payments made prior to this date but on or after July 17, 2006, for Eligible Expenditures under Categories (1)(a), (1)(b) and (1)(c).
2. The Closing Date is February 1, 2009.

APPENDIX

Definitions

1. “Beneficiary” means, within the Project Area, Community Based Organization (CBO), village organization, self-help women group, credit group or any other group eligible pursuant to Part B.1 of Schedule 2 to the Project Agreement and other eligibility criteria as set forth in the Operational Manual.
2. “Block Grants” means grants made or proposed to be made by the Recipient, out of the proceeds of the Grant, to Beneficiaries to finance the costs of goods, works and services for Sub-Projects under Part A, B or C of the Project.
3. “Category” means a category set forth in the table in Section IV of Schedule 2 to this Agreement.
4. “Consultant Guidelines” means the “Guidelines: Selection and Employment of Consultants by World Bank Borrowers” published by the Bank in May 2004.
5. “DDC” means a District Development Committee established in each district of the Recipient’s territory under the Local Self Governance Act, 2055 (1999).
6. “Environmental Assessment” means the Recipient’s environmental assessment, in form and substance satisfactory to the Association, dated March 7, 2004, which was prepared for the Original Project and shall also be used for the Project, including, *inter alia*: (i) the identification and assessment of the potential environmental impact of activities to be carried out under Sub-Projects; (ii) an evaluation of alternative measures; (iii) the EMF detailing the appropriate mitigation, monitoring, institutional and management measures required for the implementation of Sub-Projects with a view to ensuring compliance of the activities referred to in sub-paragraph (i) herein with said measures and to eliminating adverse environmental impacts, offsetting such impacts, or reducing them to acceptable levels.
7. “EMF” means the Recipient’s Environmental Management Framework which sets out, *inter alia*: (i) key principles for environmental management of Sub-Projects; (ii) procedures to screen and process Sub-Projects for significant environmental impacts, and to assist in mitigating impacts; and (iii) procedures to ensure that these principles and procedures are properly applied.
8. “Financial Management Manual” means the Financial Management Manual to be prepared by PAF pursuant to Section 5.01 of this Agreement, containing financial management guidelines for the Project, as the same may be amended from time to time with the agreement of the Association.

9. “Fiscal Year” or “FY” means the twelve (12)-month period corresponding to any of the Recipient’s and PAF’s fiscal years, which period commences and ends in mid-July of each calendar year.
10. “General Conditions” means the “International Development Association General Conditions for Credits and Grants” dated July 1, 2005.
11. “IGSP” means an Income Generating Sub-Project financed or proposed to be financed under Part A of the Project.
12. “Incremental Operating Costs” means, salaries, per diem, and fringe benefits of staff appointed to posts in PAF 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, fuels, 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, stationery, rent and utilities.
13. “Innovative Grants” means Block Grants made by PAF to selected Beneficiaries under Part C of the Project.
14. “Nepalese Rupee” and the sign “NRs” mean the currency of the Recipient.
15. “Operational Manual” means the Operational Manual to be prepared by PAF pursuant to Section 5.01 of this Agreement, containing PAF’s eligibility criteria and appraisal, approval and supervision rules and procedures for POs, Beneficiaries and Sub-Projects, as well as EMF, VCDP and negative list of Sub-Projects, and the Financial Management Manual, as the same may be amended from time to time with the agreement of the Association.
16. “Original Financing Agreement” means the Development Grant Agreement for the Poverty Alleviation Fund Project between the Recipient and the Association dated September 14, 2004 (Grant Number H091-NEP), as amended to the date of this Agreement.
17. “Original Project” means the Project described in the Original Financing Agreement.
18. “PAF” means the Poverty Alleviation Fund, an autonomous institution established pursuant to the Recipient’s Poverty Alleviation Fund Ordinance, 2004.
19. “PO” or “Partner Organization” means a Non-governmental Organization (NGO), VDC, DDC, CBO or private sector institution or entity, involved in

poverty alleviation work, which meets the eligibility criteria for POs set forth in the Operational Manual.

20. “PO Agreement” means an agreement to be entered into between PAF and a PO pursuant to Part A of Schedule 2 to the Project Agreement.
21. “Procurement Guidelines” means the “Guidelines for Procurement under IBRD Loans and IDA Credits” published by the Bank in May 2004.
22. “Procurement Plan” means the Recipient’s procurement plan for the Project, dated September 14, 2006, and referred to in paragraph 1.16 of the Procurement Guidelines and paragraph 1.24 of the Consultant Guidelines, as the same shall be updated from time to time in accordance with the provisions of said paragraphs.
23. “Project Area” means: (i) the six (6) districts that have been identified for the purpose of carrying out the Original Project, namely, Darchula, Mugu, Kapilvastu, Pyuthan, Ramechchap and Siraha; (ii) the nineteen (19) districts that have been identified for the purpose of carrying out the Project, namely, Achham, Baitadi, Bajhang, Bajura, Dadeldhura, Dailekh, Dolpa, Doti, Humla, Jajorkot, Jumla, Kalikot, Mahottari, Rasuwa, Rautahat, Rolpa, Rukum, Sarlahi and Sindhuli; and (iii) any other districts that may be identified from time to time by agreement between the Recipient and the Association for the purpose of carrying out the Project.
24. “Project Implementing Entity” means PAF.
25. “Project Implementing Entity’s Legislation” means the Recipient’s Poverty Alleviation Fund Ordinance, 2004.
26. “SSIP” means a Small-Scale Community Infrastructure Development Project financed or proposed to be financed under Part B of the Project.
27. “Sub-Project” means an IGSP, SSIP or a development project or scheme to be carried out by a community under Part A, B or C of the Project, which meets the eligibility criteria to receive financing in the form of Block Grants.
28. “Sub-Project Grant Agreement” means an agreement to be entered into between PAF and a Beneficiary pursuant to paragraph 3(b) of Part B of Schedule 2 to the Project Agreement.
29. “Subsidiary Grant Agreement” means the agreement referred to in Section I, Part A of Schedule 2 to this Agreement pursuant to which the Recipient shall make the proceeds of the Financing available to the Project Implementing Entity.

30. “VCDP” means Vulnerable Communities People’s Development Plan/Operational Guidelines dated March 7, 2004, which was prepared by the Recipient for the Original Project and shall also be used for the Project, describing a program of actions, measures and policies designed to maximize the benefits accruing to vulnerable people, as the same may be revised from time to time in agreement with the Association.
31. “VDC” means a Village Development Committee established within the Recipient’s territory pursuant to the Local Self Governance Act, 2055 (1999).