

Public Disclosure Authorized

CONFIRMED COPY

IDA GRANT NUMBER H100 KE

Development Grant Agreement

(Nairobi Water and Sewerage Institutional Restructuring Project)

between

REPUBLIC OF KENYA

and

INTERNATIONAL DEVELOPMENT ASSOCIATION

Dated June 25, 2004

Public Disclosure Authorized

IDA GRANT NUMBER H100 KE

DEVELOPMENT GRANT AGREEMENT

AGREEMENT, dated June 25, 2004, between REPUBLIC OF KENYA (the Recipient) and INTERNATIONAL DEVELOPMENT ASSOCIATION (the Association).

WHEREAS (A) the Association has received a letter from the Recipient, dated April 16, 2004, 2004, describing a program of actions, objectives and policies designed to reform and improve its water supply and sanitation sector (the Program) and declaring the Recipient's commitment to the execution of the Program in order, *inter alia*, to achieving its poverty reduction goals; and

(B) the Recipient, having satisfied itself as to the feasibility and priority of the Project described in Schedule 2 to this Agreement (the Project), has requested the Association to assist in the financing of the Project;

(C) the Project will be carried out by Nairobi Water Services Board (NWSB) and Nairobi City Water and Sewerage Company (NWSC) with the Recipient's assistance and, as part of such assistance, the Recipient will make available to NWSB and NWSC the proceeds of the grant provided for in this Agreement as provided in this Agreement; and

WHEREAS the Association has agreed, on the basis, *inter alia*, of the foregoing, to extend the Grant to the Recipient upon the terms and conditions set forth in this Agreement and in the agreements of even date herewith between the Association and NWSB (the NWSB Project Agreement) and between the Association and NWSC (the NWSC 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), with the modifications set forth in Schedule 4 to this Agreement (the General Conditions), constitute an integral part of this Agreement.

Section 1.02. Wherever used in this Agreement, unless the context otherwise requires, the several terms defined in the General Conditions and in the Recitals to this

Agreement have the respective meanings therein set forth and the following additional terms have the following meanings:

- (a) “CIP” means Capital Investment Program;
- (b) “eligible expenditures”: means the same as set forth in paragraph 1(b) of Schedule 3 to this Agreement;
- (c) “Financial Monitoring Report” or “FMR” means each report prepared in accordance with Section 4.02 of the Project Agreements;
- (d) “Framework Documents” means the Tripartite Agreement, License, SPA and Operational Assets Agreement, as each of them is defined in this Section;
- (e) “FY” means the Fiscal Year of NWSB and NWSC commencing July 1 of each calendar year and ending on June 30 of the following calendar year;
- (f) “Grant” means the financing provided for to the Recipient for the Project under Section 2.01 of this Development Grant Agreement;
- (g) “Initial Deposit” means the deposit referred to in Section 2.03 (b) of the Project Agreements;
- (h) “License” means the formal license to be issued by WSRB under the laws of the Recipient to NWSB for providing water services under the Project;
- (i) “MOF” means the Ministry of Finance of the Recipient;
- (j) “MWRMD” Ministry of Water Resources Management and Development of the Recipient;
- (k) “NCC” means City Council of Nairobi;
- (l) “NWSB” means Nairobi Water Services Board established under the Water Act;
- (m) “NWSB Project Agreement” means the agreement of even date herewith between the Association and NWSB, as such agreement may be amended from time to time; and such term includes all schedules and agreements supplemental to the NWSB Project Agreement;
- (n) “NWSB Project Account” means the account opened by NWSB pursuant to Section 2.03 (a) of the NWSB Project Agreement;

(o) “NWSB Subsidiary Grant Agreement” means the Agreement between the Recipient and NWSB referred to in Section 3.01 (b)(i) of this Agreement;

(p) “NWSC” means Nairobi City Water and Sewerage Company, Limited, established under the Companies Act, Chapter 486 (1962) of the Recipient as revised in 1972;

(q) “NWSC Project Agreement” means the agreement of even date herewith between the Association and NWSC, as such agreement may be amended from time to time; and such term includes all schedules and agreements supplemental to the NWSC Project Agreement;

(r) “NWSC Project Account” means the account opened by NWSC pursuant to Section 2.03 (a) of the NWSC Project Agreement;

(s) “NWSC Subsidiary Grant Agreement” means the Agreement between the Recipient and NWSC referred to in Section 3.01 (b)(ii) of this Agreement;

(t) “Operating Account” means each of the accounts referred to in Section 2.02 (c) of this Agreement;

(u) “Operational Assets Agreement” means the agreement between NCC and NWSC to transfer the operational assets and liabilities and WSD staff to NWSC;

(v) “Project Agreement” means either the NWSB Project Agreement or the NWSC Project Agreement as the context may require;

(w) “Project Agreements” means, collectively, the NWSB Project Agreement and NWSC Project Agreement;

(x) “PIM” means the Project Implementation Manual referred to in Section 3.03 of this Agreement;

(y) “Project Segment/ Segment” means parts of the Project as classified into segments A, B and C set forth in Section 1.03 of this Agreement in order to delineate the responsibility of NWSB and NWSC, respectively, as the Project Implementing entity for the implementation of various parts of the Project, and “Project Segments/ Segments” means, collectively, more than one Segment;

(z) “Special Account A” means the Special Account for NWSB and referred to in Section 2.02 (b) of this Agreement;

(aa) “Special Account B” means the Special Account for NWSC and referred to in Section 2.02 (b) of this Agreement;

(bb) “Special Accounts” means Special Accounts A and B referred to in Section 2.02(b) of this Agreement;

(cc) “Subsidiary Grant Agreements” means, collectively, the “NWSB Subsidiary Grant Agreement” and “NWSC Subsidiary Grant Agreement” referred to in Section 3.01 (b) of this Agreement;

(dd) “SPA” means Service Provision Agreement between NWSB and NWSC referred to in Section I, paragraph 3 of Schedule 2 to the NWSB Project Agreement;

(ee) “Tripartite Agreement” means the agreement among NWSB, NCC and NWSC to vest the assets held by NCC into NWSB;

(ff) “Water Act” means the Recipient’s Law No. 8 of 2002, as it may be amended, from time to time;

(gg) “WSD” means the Water and Sewerage Department of NCC;

(hh) “WSRB” means the Water Services Regulatory Board established under the Water Act and referred to in Section 3.02 (c) of this Agreement; and

(ii) “WSS” means Water Supply and Sewerage services in Nairobi.

Section 1.03. Each reference in the General Conditions to the Project implementation entity shall be deemed as a reference to:

(a) NWSB for Project Segment A comprising: Parts A.1; B.1(e), B.2(a), B.2(c), B.2(e), B.3(a), B.3(b) and B.3(c), C.1, C.2(a), C.2(c), C.2(d), C.2(e), C.3 of the Project;

(b) NWSB for Project Segment B comprising: Parts B.1(e), B.3(a), B.3(b) and B.3(c) of the Project (Project Segment B);

(c) NWSC for Project Segment C comprising: (i) Parts A.2; B.1(a), B.1(b), B.1(c) and B.1(d), and Parts B.2(b) and B.2(d); Part C.2(b) of the Project.

ARTICLE II

The Grant

Section 2.01. The Association agrees to make available to the Recipient, on the terms and conditions set forth or referred to in this Agreement, an amount in various currencies equivalent to ten million two hundred thousand Special Drawing Rights (SDR 10,200,000).

Section 2.02. (a) The amount of the Grant may be withdrawn from the Grant 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 carrying out the Project and to be financed out of the proceeds of the Grant.

(b) The Recipient may, for the purposes of the Project, open and maintain in Dollars two separate special deposit accounts set forth herein:

- (i) Special Account A, managed by the Recipient on behalf of NWSB; and
- (ii) Special Account B, managed by the Recipient on behalf of NWSC,

in a commercial bank or commercial banks on terms and conditions satisfactory to the Association, including appropriate protection against set off, seizure or attachment. Deposits into, and payments out of, the Special Accounts shall be made in accordance with the provisions of Schedule 3 to this Agreement.

- (c)
 - (i) The Recipient shall open or cause to be opened and maintain or cause to be maintained in Dollars an Operating Account each for NWSB and NWSC, in one or more commercial banks, on terms and conditions satisfactory to the Association (including appropriate protection against set-off, seizure or attachment).
 - (ii) The Recipient shall, in accordance with procedures acceptable to the Association, withdraw from time to time from the respective Special Account and deposit into each Operating Account, an amount required to finance eligible expenditures for a period of 90 days of Project implementation.
 - (iii) Payments out of the respective Operating Account shall only be made for eligible expenditures.
 - (iv) In the event that the Association, after consultation with the Recipient, determines that any outstanding amount in any Operating Account is not further required to cover payments for

eligible expenditures, the Recipient, upon notice from the Association shall promptly refund such outstanding amount to the respective Special Account.

Section 2.03. (a) The Recipient shall pay to the Association a commitment charge on the principal amount of the Grant 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 Recipient from the Grant 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 2.04 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 Recipient; 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 Section 4.02 of the General Conditions.

Section 2.04. Commitment charges shall be payable semiannually on January 15 and July 15 in each year.

Section 2.05. The Closing Date shall be June 30, 2007 or such later date as the Association shall establish. The Association shall promptly notify the Recipient of such later date.

ARTICLE III

Execution of the Project

Section 3.01. (a) The Recipient 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 this Agreement, shall cause: (i) NWSB to carry out Segments A and B of the Project; and (ii) NWSC to carry out Segment C of the Project, with due diligence and efficiency and in conformity with appropriate administrative, financial and public utilities practices, and to perform in accordance with the provisions of their respective Project Agreement all their obligations therein set forth, take and cause to be taken all action, including the provision of funds, facilities, services and other resources, necessary or appropriate to enable NWSB and NWSC to perform such obligations, and shall not take or permit to be taken any action which would prevent or interfere with such performance; and

(b) For the purpose of carrying out:

(i) Segments A and B of the Project, the Recipient shall make available to NWSB the proceeds of the Grant allocated from time to time to Categories 1(a), 2(a), 3(a), 4 (a) and 5(a); of the table set forth in paragraph 1 of Schedule 1 to this Agreement, under a subsidiary grant agreement to be entered into between the Recipient and NWSB, under terms and conditions which shall have been approved by the Association; and

(ii) Segment C of the Project, the Recipient shall make available to NWSC the proceeds of the Grant allocated from time to time to Categories 1(b), 2(b), 3(b), 4 (b) and 5(b) of the table set forth in paragraph 1 of Schedule 1 to this Agreement, under a subsidiary grant agreement to be entered into between the Recipient and NWSC, under terms and conditions which shall have been approved by the Association.

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

Section 3.02. The Recipient shall ensure that:

(a) NWSB Project Account shall be provided with a cash balance of no less than twelve million Kenyan Shillings (KES 12,000,000) by the date of effectiveness of this Agreement

(b) NWSC Project Account shall be provided with a cash balance of no less than twenty two million Kenyan Shillings (KES 22,000,000) by the date of effectiveness of this Agreement.

(c) To enable NWSB to provide service, WSRB shall issue the License, satisfactory to the Association, to NWSB in a timely manner.

Section 3.03. The Recipient shall jointly with NWSB and NWSC prepare and adopt and furnish to the Association a PIM, satisfactory to the Association. The said PIM shall, *inter alia*, include: (i) a Project implementation plan; (ii) a Project monitoring and evaluation plan; (iii) a Project procurement plan; (iv) a Project financial management manual; and (v) such other administrative, financial, technical and organizational arrangements as shall be required for the Project. Except as the Association may otherwise agree, the Recipient shall not amend, abrogate or waive any provision of said PIM.

Section 3.04. MWRMD shall have published a complete plan, satisfactory to the Association, for the transfer of the management and operation of water services to NWSB as per the provision of Section 113 of the Water Act within one year from the Date of Effectiveness of this agreement.

Section 3.05. The Recipient and the Association hereby agree that the obligations set forth in Sections 9.03, 9.04, 9.05, 9.06, 9.07 and 9.08 of the General Conditions (relating to insurance, use of goods and services, plans and schedules, records and reports, maintenance and land acquisition, respectively) in respect of Segments A and B of the Project shall be carried out by NWSB and in respect of Segment C of the Project by NWSC pursuant to Section 2.03 of the Project Agreements.

ARTICLE IV

Financial Covenants

Section 4.01. (a) The Recipient shall establish and maintain or cause NWSB and NWSC to establish and maintain a financial management system, including records and accounts, and prepare financial statements, all in accordance with consistently applied accounting standards acceptable to the Association, adequate to reflect its operations, resources and expenditures related to the Project.

(b) The Recipient shall itself or shall cause NWSB and NWSC to:

- (i) have the financial statements referred to in paragraph (a) of this Section and those for the Special Accounts for each fiscal year (or other period agreed to by the Association), audited, in accordance with consistently applied auditing standards acceptable to the Association, 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 (or such other period agreed to by the Association), (A) certified copies of the financial statements referred to in paragraph (a) of this Section for such year (or such other period agreed to by the Association), as so audited, and (B) an opinion on such statements by said auditors, in scope and detail satisfactory to the Association; and
 - (iii) furnish to the Association such other information concerning such records, accounts and the audit of such financial statements, and concerning said auditors, as the Association may from time to time reasonably request.
- (c) For all expenditures with respect to which withdrawals from the Grant Account were made on the basis of statements of expenditure, the Recipient shall:
- (i) 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, or covering, the fiscal year in which the last withdrawal from the Grant Account was made;
 - (ii) enable the Association's representatives to examine such records; and
 - (iii) ensure that such statements of expenditure are included in any audit that the Association may have requested pursuant to paragraph (b) of this Section.

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) NWSB shall have failed to perform any of its obligations under the NWSB Project Agreement.

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

(c) As a result of events which have occurred after the date of this Development Grant Agreement, an extraordinary situation shall have arisen which shall make it improbable that:

(i) NWSB will be able to perform its obligations under the NWSB Project Agreement; or

(ii) NWSC will be able to perform its obligations under the NWSC Project Agreement.

(d) The Water Act shall have been amended, suspended, abrogated, repealed or waived which, in the reasonable opinion of the Association, shall affect materially and adversely the ability of NWSB or NWSC to perform any of its obligations under its respective Project Agreement.

(e) The Rules made pursuant to Section 113 of the Water Act shall have provided for arrangements which, in the reasonable the opinion of the Association, grant control over WSS assets in Nairobi to an entity or entities other than NWSB.

(f) Any of the Framework Documents shall have been amended, suspended, abrogated, repealed or waived which, in the reasonable opinion of the Association, shall affect materially and adversely the ability of NWSB or NWSC to perform any of its obligations under its respective Project Agreement.

(g) The License shall have been revoked by WSRB.

ARTICLE VI

Effectiveness; Termination

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

(a) the NWSB Subsidiary Grant Agreement has been executed on behalf of the Recipient and NWSB;

(b) the NWSC Subsidiary Grant Agreement has been executed on behalf of the Recipient and NWSC;

(c) NWSB shall have opened the Project Account and shall have made the Initial Deposit referred to in Section 2.03 (b) of the NWSB Project Agreement;

(d) NWSC shall have opened the Project Account and shall have made the Initial Deposit referred to in Section 2.03 (b) of the NWSC Project Agreement;

(e) NWSB shall have appointed a Chief Executive Officer and other key management staff responsible for technical, financial, legal and administrative functions under the Project, all of qualifications and experience satisfactory to the Association; and

(f) NWSC shall have appointed a Managing Director, a Company Secretary and other key management staff responsible for technical, financial, legal and administrative functions under the Project, all of qualifications and experience satisfactory to the Association.

(g) NWSB and NWSC shall have established their financial management systems, satisfactory to the Association; and

(h) PIM shall have been adopted in accordance with the requirements of Section 3.03 of this Agreement.

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 NWSB Project Agreement has been duly authorized or ratified by NWSB, and is legally binding upon NWSB in accordance with its terms;

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

(c) that the NWSB Subsidiary Grant Agreement has been duly authorized or ratified by the Recipient and NWSB and is legally binding upon the Recipient and NWSB in accordance with its terms;

(d) that the NWSC Subsidiary Grant Agreement has been duly authorized or ratified by the Recipient and NWSB and is legally binding upon the Recipient and NWSB in accordance with its terms;

(e) that the SPA has been duly authorized or ratified by the NWSB and NWSC and is legally binding upon the parties thereto in accordance with its terms;

(f) that the Tripartite Agreement has been duly authorized or ratified by the NWSB, NCC and NWSC and is legally binding upon the parties thereto in accordance with its terms; and

(g) that the Operational Assets Agreement has been duly authorized or ratified by the NWSC and NCC and is legally binding upon the parties thereto 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 VIII

Representative of the Recipient; Addresses

Section 8.01. The Minister of Finance of the Recipient is designated as representative of the Recipient for the purposes of Section 11.03 of the General Conditions.

Section 8.02 The following addresses are specified for the purposes of Section 11.01 of the General Conditions:

For the Recipient:

The Minister of Finance
Ministry of Finance
P.O. Box 30007
Nairobi, Kenya

Cable address:	Facsimile:
FINANCE	254 2 240045
NAIROBI	254 2 219365

For the Association:

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

Cable address:	Telex:	Facsimile:
INDEVAS	248423 (MCI)	(202) 477-6391
Washington, D.C.	64145 (MCI)	

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

REPUBLIC OF KENYA

By /s/ David Mwiraria

Authorized Representative

INTERNATIONAL DEVELOPMENT ASSOCIATION

By /s/ Makhtar Diop

Authorized Representative

SCHEDULE 1

Withdrawal of the Proceeds of the Grant

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

<u>Category</u>	<u>Amount of the Grant Allocated (Expressed in SDR Equivalent)</u>	<u>% of Expenditures to be Financed</u>
(1) Works		65 %
(a) NWSB	837,000	
(b) NWSC	167,000	
(2) Goods		100%
(a) NWSB	1,605,000	
(b) NWSC	1,250,000	
(3) Consultants' services		90 %
(a) NWSB	3,624,000	
(b) NWSC	1,714,000	
(4) Training, study tours workshops and fellowships		100 %

Amount of the

<u>Category</u>	<u>Grant Allocated (Expressed in SDR Equivalent)</u>	<u>% of Expenditures to be Financed</u>
(a) NWSB	247,500	
(b) NWSC	235,500	
(5) Operating costs		80 % in First Year 60% in Second Year 40% in Subsequent years
(a) NWSB	30,000	
(b) NWSC	380,000	
(6) Unallocated	110,000	
TOTAL	<u>10,200,000</u>	

2. For the purposes of this Schedule:

(a) the term “foreign expenditures” means expenditures in the currency of any country other than that of the Recipient for goods or services supplied from the territory of any country other than that of the Recipient;

(b) the term “local expenditures” means expenditures in the currency of the Recipient or for goods or services supplied from the territory of the Recipient; and

(c) the term “operating costs” means funds provided to support the initial working capital of NWSB and NWSC including costs associated with the purchases of chemical, electricity, utilities, office supplies, consumables, fuel, and maintenance of vehicles.

3. It is understood that the percentages of expenditures to be financed under the table set forth in paragraph 1 of this Schedule have been calculated on the basis of the provision of a letter issued by the Recipient’s Ministry of Finance pursuant to Section 138 (1) and (2) (g) of The Customs and Excise Act and Section 23 (1) and 3 (e) of the VAT Act, as read together with the Legal Notice Number 138 (The Customs and Excise

Act, Chapter 472) and Legal Notice No. 145 (VAT Act, Chapter 476) both of 4th June, 1992 (as amended in 1996 and 2001) of the Recipient, which provides for exemption of taxes levied in the territory of the Recipient on works, goods and services for this Project. If any change is made to said Letter and Acts or Legal Notices, which has the effect of levying taxes or customs duties on such works, goods and services, the percentages referred to above shall be decreased in accordance with the provisions of Section 5.08 of the General Conditions.

4. 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.

5. The Association may require withdrawals from the Grant Account to be made on the basis of statements of expenditure for expenditures for: (a) all operating costs; (b) training, study tours and workshops; (c) goods under contracts not exceeding \$150,000 equivalent; (d) works under contracts not exceeding \$200,000 equivalent; (e) consulting firms under contracts not exceeding \$100,000 equivalent; and (f) individuals consultants not exceeding \$50,000 equivalent, under such terms and conditions as the Association shall specify by notice to the Recipient.

6. If the Association shall have determined at any time that any amount of the Grant was used in a manner inconsistent with the provisions of this Agreement, the Recipient shall, promptly upon notice from the Association, refund to the Association for deposit into the Grant Account, an amount equivalent to the amount so used.

SCHEDULE 2

Description of the Project

The objective of the Project is to build a strong governance, institutional and service delivery framework by providing support for the implementation of Water Act so as to enable efficient and sustainable delivery of water and sewerage services to the population of Nairobi. To this effect, the Project will support the operationalization and strengthening of new autonomous and ring-fenced service provision utilities.

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.

Part A: Institutional Strengthening of New Service Delivery Framework

Operationalization and strengthening of: (a) NWSB; and (b) NWSC through:

1. Operationalization and Strengthening of NWSB

(a) refurbishment of office space including the space partitioning and purchase of necessary office furniture;

(b) purchase of vehicles;

(c) purchase of office equipment comprising computers, photocopiers and relevant accessories;

(d) provision for incremental operating costs of NWSB, including utility expenses, communication cost and report production cost;

(e) technical assistance including a range of consultancy services in the areas utility management, financial management, infrastructure planning and procurement, environmental management and legal advice; and

(f) training and capacity building including targeted workshops, courses and study tours for the members of the NWSB's Board of Directors and the staff of the Board.

2. Operationalization and Strengthening of NWSC

(a) Refurbishment of corporate headquarters at Kampala Road, Nairobi, and the six areas offices and other service facilities including laboratories and production and sewerage plant offices;

(b) purchase of about 10 operational vehicles for the corporate head office and the six area offices;

(c) purchase of office equipment comprising computers, photocopiers and accessories relevant for the corporate head office and the area offices under the Project;

(d) provision for incremental operating costs of NWSC, including utility expenses, communication cost and report production cost;

(e) technical assistance in a range of consultancy services in the areas utility management, financial management, commercial management, environmental management; and

(f) training and capacity building including targeted workshops, courses and study tours for the members of the Board of Directors and the staff of NWSC.

3. Technical Assistance for WSRB Activities

(a) provision of technical assistance for WSRB to review the regulatory design and any potential tariff adjustments with regards to the Nairobi WSS service provision; and

(b) provision of technical assistance for WSRB to carry out data collection and analysis of consumer and social protection concerns with regards to services to the poor and propose mitigation measures for compliance by NWSB and NWSC.

Part B: Immediate Service Delivery Improvement Program

Support for the selected activities aimed at strengthening the commercial, financial and technical operations of WSS operations in Nairobi with specific focus on strengthening the commercial operations of about six area/business centers through:

1. Improvements in Commercial Operations

(a) provision to carry out a comprehensive customer survey, GIS based block mapping and development of a customer care program;

(b) purchase and installation of a comprehensive commercial billing and customer care system;

(c) introduction of a new Geographical Information System (GIS) linked billing system and customer care program in all six business centers;

(d) support for the customer care program through an appropriate Information Technology (IT) and communication platform and a necessary equipment, services, and communication system; and

(e) purchase and installation of bulk and zonal meters at all major nodes of the WSS network as well as the purchase of approximately 15,000 new customer meters.

2. Improvement of Financial Operations

(a) purchase and introduction of a financial management software for NWSB;

(b) purchase and introduction of a financial management software for NWSC;

(c) consultant services to improve the financial management and record systems of NWSB;

(d) consultant services to improve the financial management and record systems of NWSC; and

(e) services for carrying out an assets reevaluation of all movable and non-movable assets of the Nairobi WSS systems.

3. Improvement of Technical Operations

(a) purchase of essential spare parts for various categories of electro-mechanical equipment and operational equipment needed for the Project;

(b) carrying out minor civil works aimed at reduction of unaccounted for water, including replacing appurtenances on the transmission mains and removal of system bottlenecks in the distribution system; and

(c) hiring services needed for the modeling of the WSS network to enhance programmed operations and maintenance.

Part C: Monitoring and Evaluation, Consultation and Communications, and Preparation of Follow-on Program

Support for monitoring and evaluation of the Project activities, implementation of a complementary communication program for institutional transformation in service provision as well as provide support for the preparation of follow-on WSS investment plans in Nairobi and Mombasa through the provision for:

1. Project Monitoring and Evaluation

(a) annual independent financial audits of the Project by the appropriate National Audit Agency of the Recipient, acceptable to the Association;

(b) systematic quarterly technical, financial and operation performance reviews of NWSB and NWSC; and

(c) mandatory mid-term review and final review of the Project.

2. Stakeholder Consultation and Communication Campaign

(a) implementation by NWSB of suitable multi-media communication strategy and campaign on the new WSS service arrangements under the Project;

(b) implementation by NWSC of suitable multi-media communication strategy and campaign on the new WSS service arrangements under the Project;

(c) financial support for the participation of stakeholders at the annual Project performance review workshops;

(d) financial support for donor consultation for Nairobi and Mombasa; and

(e) carrying out thematic consultation concerning specific aspects of the process and outputs of the CIP for Nairobi, Mombasa and possibly other urban centers.

3. Preparation of the follow-on WSS Program

technical assistance for the preparation of CIP for Nairobi and Mombasa and possibly other urban centers covering: (a) water resources assessment; (b) services demand and investment forecast; (c) institutional and legal review; (d) capacity building and institutional development; (e) environment and social assessment and mitigation plan; and (f) preparation of tender documents for a follow-on project.

* * *

The Project is expected to be completed by December 31, 2006.

SCHEDULE 3

Special Accounts

1. For the purposes of this Schedule:

(a) the term “eligible Categories” means: (i) Categories 1(a), 2(a), 3(a), 4 (a) and 5(a) in respect of Special Account A for Segments A and B of the Project; (ii) Categories 1(b), 2(b), 3(b), 4 (b) and 5(b) in respect of Special Account B for Segment C of the Project; set forth in the table in paragraph 1 of Schedule 1 to this Agreement;

(b) the term “eligible expenditures” means expenditures in respect of the reasonable cost of goods and services required for the Project and to be financed out of the proceeds of the Grant allocated from time to time to the eligible Categories in accordance with the provisions of Schedule 1 to this Agreement; and

(c) the term “Authorized Allocation” means with respect to the Special Account A, an amount equivalent to \$ 1,500,000; and with respect to the Special Account B an amount equivalent to \$1,000,000 , to be withdrawn from the Grant Account and deposited into the Special Accounts pursuant to paragraph 3 (a) of this Schedule, provided, however, that unless the Association shall otherwise agree, the Authorized Allocation shall be limited to an amount equivalent to \$750,000 in respect of the Special Account A; and an amount equivalent to \$500,000 in respect of the Special Account B, until the aggregate amount of withdrawals from the Grant Account plus the total amount of all outstanding special commitments entered into by the Association pursuant to Section 5.02 of the General Conditions shall be equal to or exceed the equivalent of SDR 3,500,000.

2. Payments out of the respective Special Accounts shall be made exclusively for eligible expenditures in accordance with the provisions of this Schedule.

3. After the Association has received evidence satisfactory to it that the respective Special Account has been duly opened, withdrawals of the Authorized Allocation and subsequent withdrawals to replenish the respective Special Account shall be made as follows:

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

- (b) (i) For replenishment of the respective Special Account, the Recipient shall furnish to the Association requests for deposits into the respective Special Account at such intervals as the Association shall specify.
- (ii) Prior to or at the time of each such request, the Recipient shall furnish to the Association the documents and other evidence required pursuant to paragraph 4 of this Schedule for the payment or payments in respect of which replenishment is requested. On the basis of each such request, the Association shall, on behalf of the Recipient, withdraw from the Grant Account and deposit into the respective Special Account such amount as the Recipient shall have requested and as shall have been shown by said documents and other evidence to have been paid out of the respective Special Account for eligible expenditures. All such deposits shall be withdrawn by the Association from the Grant Account under the respective eligible Categories, and in the respective equivalent amounts, as shall have been justified by said documents and other evidence.

4. For each payment made by the Recipient out of the respective Special Account, the Recipient shall, at such time as the Association shall reasonably request, furnish to the Association such documents and other evidence showing that such payment was made exclusively for eligible expenditures.

5. Notwithstanding the provisions of paragraph 3 of this Schedule, the Association shall not be required to make further deposits into any Special Account:

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

(b) if the Recipient shall have failed to furnish to the Association, within the period of time specified in Section 4.01 (b) (ii) of this Agreement, any of the audit reports required to be furnished to the Association pursuant to said Section in respect of the audit of the records and accounts for the Special Accounts;

(c) if, at any time, the Association shall have notified the Recipient of its intention to suspend in whole or in part the right of the Recipient to make withdrawals from the Grant Account pursuant to the provisions of Section 6.02 of the General Conditions; or

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

Thereafter, withdrawal from the Grant Account of the remaining unwithdrawn amount of the Grant allocated to the eligible Categories shall follow such procedures as the Association shall specify by notice to the Recipient. 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 respective Special Account as of the date of such notice will be utilized in making payments for eligible expenditures.

6. (a) If the Association shall have determined at any time that any payment out of any Special Account: (i) was made for an expenditure or in an amount not eligible pursuant to paragraph 2 of this Schedule; or (ii) was not justified by the evidence furnished to the Association, the Recipient shall, promptly upon notice from the Association: (A) provide such additional evidence as the Association may request; or (B) deposit into the respective Special Account (or, if the Association shall so request, refund to the Association) an amount equal to the amount of such payment or the portion thereof not so eligible or justified. Unless the Association shall otherwise agree, no further deposit by the Association into any Special Account shall be made until the Recipient has provided such evidence or made such deposit or refund, as the case may be.

(b) If the Association shall have determined at any time that any amount outstanding in any Special Account will not be required to cover further payments for eligible expenditures, the Recipient shall, promptly upon notice from the Association, refund to the Association such outstanding amount.

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

(d) Refunds to the Association made pursuant to paragraphs 6 (a), (b) and (c) of this Schedule shall be credited to the Grant Account for subsequent withdrawal or for cancellation in accordance with the relevant provisions of this Agreement, including the General Conditions.

SCHEDULE 4

Modifications to the General Conditions

For the purpose of this Agreement, the provisions of the General Conditions are modified as follows:

1. Sections 3.02, 3.03, 3.04(a), 3.04(b), 3.05, 6.05, Article VII, are deleted in their entirety.

2. Wherever used in the General Conditions, the following terms are modified to read as follows:

- (a) The term “Borrower” is modified to read “Recipient”.
- (b) The term “Credit” is modified to read “Grant”.
- (c) The term “credit” is modified to read “grant”; except that where used in Sections 6.02(a)(ii) and 6.02(c)(i), as modified below, the term “credit” shall continue to read “credit”.
- (d) The term “Credit Account” is modified to read “Grant Account”.
- (e) The term “Development Credit Agreement” is modified to read “Development Grant Agreement”.

3. Article IV is modified as follows:

(a) Section 4.02(a) and the heading of Section 4.02 are modified to read as follows:

“Section 4.02. Currencies in which Commitment Charges are Payable

- (a) The Recipient shall pay the commitment charge on the Grant in the currency specified in the Development Grant Agreement or in such other eligible currency or currencies as may from time to time be designated or selected pursuant to paragraph (c) or (e) of this Section.”
- (b) Wherever used in Section 4.02(c) and (e) of the General Conditions the words “principal and service charges” are modified to read “commitment charge”.
- (c) Section 4.03 and its heading are modified to read as follows:

“Section 4.03. Amount of the Grant

The amount of the Grant withdrawn from time to time shall be the equivalent in terms of SDR (determined as of the date or respective dates of withdrawal from the Grant Account) of the value of the currency or currencies so withdrawn.”

4. Section 6.02 is modified as follows:
 - (a) The phrase “any other development credit agreement” in Section 6.02(a)(ii) is modified to read: “any other development grant agreement or any development credit agreement or development financing agreement”.
 - (b) The phrase “any development credit agreement” in Section 6.02(c)(i) is modified to read: “any development grant agreement, development credit agreement or development financing agreement”.
5. The words “The principal of, and any other charges on” in paragraph (a) of Section 8.01 are modified to read “The commitment charge on”.
6. Section 12.05 and its heading are modified to read as follows:

“Section 12.05. Termination of Development Grant Agreement.

The obligations of the Recipient under the Development Grant Agreement shall terminate on the date 20 years after the date of the Development Grant Agreement.”