

CONFORMED COPY

CREDIT NUMBER 3773 UG

GRANT NUMBER H041 UG

Development Financing Agreement

(Second Local Government Development Project)

between

THE REPUBLIC OF UGANDA

and

INTERNATIONAL DEVELOPMENT ASSOCIATION

Dated June 20, 2003

CREDIT NUMBER 3773 UG

GRANT NUMBER H041 UG

DEVELOPMENT FINANCING AGREEMENT

AGREEMENT, dated June 20, 2003, between THE REPUBLIC OF UGANDA (the Borrower) and INTERNATIONAL DEVELOPMENT ASSOCIATION (the Association).

WHEREAS (A) the Association has received a letter from the Borrower, dated March 17, 2003, describing a program designed to improve fiscal decentralization, the control and management of public expenditure, and to strengthen the fiscal and institutional capacity of its local governments to provide improved basic public services (the Program) and declaring the Borrower's commitment to the execution of the Program;

(B) 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;

(C) the Borrower intends to obtain from: (i) Republic of Ireland (Ireland Aid) a grant in an amount equivalent to seven million five hundred thousand US dollars (US\$7,500,000) (the Irish Cofinancing); (ii) Republic of Austria (Austrian Development Cooperation) a grant in an amount equivalent to three hundred thousand US dollars (US\$300,000) (the Austrian Cofinancing); (iii) Kingdom of Denmark (Danish International Development Assistance (DANIDA)) a grant in an amount equivalent to two million four hundred thousand US dollars (US\$2,400,000) (the DANIDA Cofinancing); and (iv) Kingdom of Netherlands a grant in an amount equivalent to fifteen million US dollars (US\$15,000,000) (the Dutch Cofinancing), all to assist in financing the Project on the terms and conditions set forth in agreements to be entered into between: (i) the Borrower and Ireland Aid; (ii) the Borrower and Austrian Development Cooperation; (iii) the Borrower and DANIDA; and (iv) the Borrower and Kingdom of Netherlands (the Cofinancing Agreements); and

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

NOW THEREFORE the parties hereto hereby agree as follows:

ARTICLE I

General Conditions; Definitions

Section 1.01. The “General Conditions Applicable to Development Credit Agreements” of the Association, dated January 1, 1985 (as amended through October 6, 1999), with the modifications set forth in Schedule 6 to this Agreement (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) “Capacity Building Grant” means a grant, made, or to be made, to an Eligible Local Government (as hereinafter defined) to finance a Subproject (as hereinafter defined) under Part C of the Project, pursuant to a Participation Agreement (as hereinafter defined);

(b) “District” means a district established under the Borrower’s Constitution and its Local Governments Act (as hereinafter defined);

(c) “Eligible Local Government” means a Local Government (as hereinafter defined), which is deemed to be eligible on the basis of the eligibility criteria referred to in Section 2 of the PIP (as hereinafter defined), for accessing a Local Development Grant (as hereinafter defined) or a Capacity Building Grant;

(d) “Eligible Categories” means Categories (1) through (6) set forth in the table in Part A.1 of Schedule 1 to this Agreement;

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

(f) “Environmental Impact Assessment” and “Environmental and Social Management Framework Report” means the set of mitigation, monitoring and institutional measures that have been identified to be taken during the implementation of the Project to mitigate potential adverse environmental and social impacts, offset them, reduce them to acceptable levels, or to enhance positive impacts;

(g) “Environmental Checklist” means a checklist for environmental assessment and audit of Subprojects under Part B of the Project, to eliminate any adverse environmental and social impacts, offset them, or reduce them to acceptable levels, or to enhance positive impacts;

(h) “Financial Monitoring Report” means each report prepared in accordance with Section 4.02 of this Agreement;

(i) “Fiscal Year” means the Borrower’s fiscal year, which begins on July 1 and ends on June 30 of the following year;

(j) “Higher-Level Local Government” means (for the purposes of the Project) a District, a Municipality, and the Divisions of Kampala City Council;

(k) “Institutional Plan” means a plan dated March 10, 2003 outlining the internal assignments within MOLG (as hereinafter defined) to support the implementation of the Project;

(l) “LGDP 1” means the First Local Government Development Program;

(m) “LGDP 1 Third Tranche” means the final Tranche of the proceeds of the credit allocated to category (4) (c) in the table set forth in paragraph 1 of schedule 1 to the Development Credit Agreement between the Borrower and the Association dated December 22, 1999 for the LGDP 1;

(n) “Letter of Sector Policy” means the Borrower’s letter referred to in paragraph (A) of the preamble to this Agreement;

(o) “Local Development Grant” means a grant, made, or to be made, to an Eligible Local Government to finance a Subproject (as hereinafter defined) under Part B of the Project pursuant to a Participation Agreement (as hereinafter defined);

(p) “Local Government” means a local government established under the Local Governments Act (as hereinafter defined);

(q) “Local Governments Act” means the Borrower’s Local Governments Act No.1 of 1997 as amended;

(r) “Lower-Level Local Government” means (for the purposes of the Project) a Sub-county, a Municipal Division, and a Town Council;

(s) “MOLG” means the Borrower’s Ministry of Local Government;

(t) “Participation Agreement” means each of the agreements to be entered into between the Borrower and a Higher Level Local Government for the purposes of making a Local Development Grant or a Capacity Building Grant, in accordance with the provisions of paragraph 6 of Schedule 4 to this Agreement, and of the PIP (as hereinafter defined), as the same may be amended from time to time, and such term includes all schedules to the Participation Agreement;

(u) “PCU” means the Program Coordination Unit established within MOLG for the execution of the Project;

(v) “Project Account” means the account referred to in Section 3.04 of this Agreement;

(w) “Project Implementation Plan” or “PIP” means the Project Implementation Plan adopted by the Borrower on April 22, 2003, as the same may be amended from time to time, and such term includes any schedules to the Project Implementation Plan;

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

(y) “Resettlement Policy Framework” means the framework dated February 20, 2003, outlining the modalities for land acquisition, resettlement and rehabilitation under Part B of the Project;

(z) “Special Accounts” means the accounts referred to in Part B of Schedule 1 to this Agreement; and

(aa) “Subproject” means: (i) an infrastructure investment financed, or proposed to be financed through a Local Development Grant under Part B of the Project; and (ii) an activity financed through a Capacity Building Grant under Part C of the Project, and which satisfies the eligibility criteria set forth in paragraphs 4 and 5 of Schedule 4 to this Agreement, and the PIP.

ARTICLE II

The Financing

Section 2.01. The Association agrees to make available to the Borrower, on the terms and conditions set forth or referred to in this Agreement:

(a) an amount in various currencies equivalent to thirty six million seven hundred thousand Special Drawing Rights (SDR 36,700,000) (the Credit); and

(b) an amount in various currencies equivalent to fifty five million Special Drawing Rights (SDR 55,000,000) (the Grant).

Section 2.02. The amount of the Credit may be withdrawn from the Credit Account and the amount of the Grant may be withdrawn from the Grant Account, in each case in accordance with the provisions of Schedule 1 to this Agreement for: (a) expenditures made (or, if the Association shall so agree, to be made) in respect of the reasonable cost of goods and services required for Parts A, D and E of the Project, and to be financed out of the proceeds of the Financing; and (b) amounts paid (or if the Association shall so agree, to be paid) on account of withdrawals made by a Local Government, under a Subproject (under Parts B and C of the Project) to meet the reasonable cost of goods and services required for a Subproject in respect of which withdrawals from the Credit Account or the Grant Account is requested.

Section 2.03. The Closing Date shall be June 30, 2007 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: (i) 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, such rate not to exceed the rate of one-half of one percent (1/2 of 1%) per annum; and (ii) 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, such rate not to exceed the rate of one-half of one percent (1/2 of 1%) per annum.

(b) Each 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 the Grant Account (as the case may be), or cancelled; and (ii) at the respective 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 respective rate set as of June 30 in each year shall be applied from the next date in that year specified in Section 2.07 of this Agreement.

(c) Each 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 October 15 and April 15 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 October 15 and April 15 commencing October 15, 2013 and ending April 15, 2043. Each installment to and including the installment payable on April 15, 2023 shall be one percent (1%) of such principal amount, and each installment thereafter shall be two percent (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 Bank 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 of the Credit 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.

ARTICLE III

Execution of the Project

Section 3.01. (a) The Borrower declares its commitment to the objective of the Project as set forth in Schedule 2 to this Agreement and, to this end, shall:

- (i) carry out Parts A, D, and E of the Project through MOLG with due diligence and efficiency and in conformity with appropriate administrative, financial and environmental practices, and shall provide, promptly as needed, the funds, facilities, services and other resources required for the Project; and
- (ii) cause Eligible Local Governments to carry out Parts B and C of the Project, with due diligence and efficiency and in conformity with appropriate administrative, financial, environmental practices and technical practices, and shall provide, promptly as needed, the funds, facilities, services and other resources required to enable Eligible Local Governments to carry out Parts B and C of the Project, and shall not take or permit to be taken any action which would prevent or interfere with

the carrying out of Parts B and C of the Project by Eligible Local Governments.

(b) Without limitation upon the provisions of paragraph (a) of this Section and except as the Borrower and the Association shall otherwise agree, the Borrower shall carry out Parts A, D and E of the Project, and cause Eligible Local Governments to carry out Parts B and C of the Project, in accordance with the implementation program set forth in Schedule 4 to this Agreement.

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 Financing shall be governed by the provisions of Schedule 3 to this Agreement.

Section 3.03. For the purposes of Section 9.06 of the General Conditions and without limitation thereto, the Borrower shall:

(a) prepare, on the basis of guidelines acceptable to the Association, and furnish to the Association not later than six (6) months after the Closing Date or such later date as may be agreed for this purpose between the Borrower and the Association, a plan for the future operation of the Project; and

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

Section 3.04. Without limitation to its obligations under Section 3.01 of this Agreement, the Borrower shall:

(a) open and maintain an account (the Project Account) in Uganda Shillings in a commercial bank on terms and conditions satisfactory to the Association;

(b) promptly thereafter: (i) make an initial deposit into such account, the Uganda Shillings equivalent to \$ 250,000; and (ii) not later than December 31, 2003 deposit into such account, the Uganda Shillings equivalent to \$250,000, all to finance the Borrower's contribution to the Project;

(c) thereafter deposit into the Project Account by December 1, March 1, June 1 and September 1 in each year during the Project implementation, such amounts as shall be required to timely replenish the Project Account back to the amount of the initial deposit referred to in paragraph (b) of this Section 3.04; and

(d) ensure that the amounts deposited into the Project Account shall be used exclusively to meet the expenditures made or to be made in respect of the reasonable cost of goods and services under the Project.

ARTICLE IV

Financial Covenants

Section 4.01. (a) The Borrower shall maintain a financial management system, including records and accounts, and prepare financial statements in a format acceptable to the Association, adequate to reflect the operations, resources and expenditures related to the Project.

(b) The Borrower shall:

- (i) have the records, accounts and financial statements referred to in paragraph (a) of this Section and the records and accounts for Special Accounts A and B for each fiscal year audited, in accordance with auditing standards acceptable to the Association, 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: (A) certified copies of the financial statements referred to in paragraph (a) of this Section for such year as so audited; and (B) an opinion on such statements, records and accounts, and the report of such audit, by said auditors, of such scope and in such detail as the Association shall have reasonably requested; and
- (iii) furnish to the Association such other information concerning such records, accounts and financial statements and the audit thereof, and concerning said auditors, as the Association shall from time to time reasonably request.

(c) For all expenditures with respect to which withdrawals from the Credit Account were Report-based disbursements or were made on the basis of statements of expenditure, the Borrower shall:

- (i) maintain or cause to be maintained, in accordance with paragraph (a) of this Section, records and separate accounts reflecting such expenditures;
- (ii) retain, 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, all records (contracts, orders, invoices, bills, receipts and other documents) evidencing such expenditures;

- (iii) enable the Association's representatives to examine such records; and
- (iv) ensure that such records and accounts are included in the annual audit referred to in paragraph (b) of this Section and that the report of such audit contains a separate opinion by said auditors as to whether the statements of expenditure or the reports referred to in Part A.5 of Schedule 1 to this Agreement, as the case may be, 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.

Section 4.02. (a) Without limitation upon the Borrower's progress reporting obligations set out in paragraphs 11 and 12 of Schedule 4 to this Agreement, the Borrower shall, prepare and furnish to the Association a financial monitoring report, in form and substance satisfactory to the Association, which:

- (i) sets forth sources and uses of funds for the Project, both cumulatively and for the period covered by said report, showing separately funds provided under the Financing and explains variances between the actual and planned uses of such funds;
- (ii) describes physical progress in Project implementation, both cumulatively and for the period covered by said report, and explains variances between the actual and planned Project implementation; and
- (iii) sets forth the status of procurement under the Project, as at the end of the period covered by said report.

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

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) A situation shall have arisen which shall make it improbable that the Program or a significant part thereof will be carried out.

(b) The Local Governments Act shall have been amended, suspended, abrogated or waived so as to materially and adversely affect the ability of the Borrower or Eligible Local Governments to perform any of their obligations.

(c) The Borrower shall have made available the proceeds of Financing allocated to Categories (5) and (6) under the table set forth in paragraph 1 of Schedule 1 to this Agreement for any purpose other than for implementation of a Subproject under Parts B and C of the Project.

(d) (i) Subject to subparagraph (ii) of this paragraph the right of the Borrower to withdraw the proceeds of the DANIDA Grant, Netherlands Grant, Austrian Grant or Ireland Aid Grant made to the Borrower for the financing of the Project shall have been suspended, canceled or terminated in whole or in part, pursuant to the terms of the agreements providing therefore.

(ii) Subparagraph (i) of this paragraph shall not apply if the Borrower establishes to the satisfaction of the Association that: (A) such suspension, cancellation, termination or prematuring is not caused by the failure of the Borrower to perform any of its obligations under such agreement; and (B) adequate funds for the Project are available to the Borrower from other sources on terms and conditions consistent with the obligations of the Borrower under this Agreement.

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

(b) the event specified in paragraph (d) (i) of Section 5.01 of this Agreement shall occur, subject to the proviso of paragraph (d) (ii) of that Section.

ARTICLE VI

Effective Date; 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 Borrower has appointed to the Program Coordination Unit a procurement specialist having experience and qualifications satisfactory to the Association, and employed in accordance with the provisions of Section II of Schedule 3 to this Agreement; and

(b) the Project Account referred to in Section 3.04 of this Agreement has been opened and an initial deposit of the Uganda Shillings equivalent of \$250,000 has been made therein.

Section 6.02. 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. The Minister of the Borrower responsible for finance 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:

Ministry of Finance, Planning and Economic Development
PO Box 8147
Kampala
Uganda

Cable address:	Facsimile:
FINSEC	256-41 230 163
Kampala	

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 the District of Columbia, United States of America, as of the day and year first above written.

THE REPUBLIC OF UGANDA

By /s/ Edith Ssempala

Authorized Representative

INTERNATIONAL DEVELOPMENT ASSOCIATION

By /s/ Pamela Cox

Authorized Representative

SCHEDULE 1

Withdrawal of the Proceeds of the Financing

A. General

1. The table below sets forth the Categories of items to be financed out of the proceeds of the Financing, the allocation of the amounts of the Credit and 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 Credit Allocated (Expressed in SDR Equivalent)</u>	<u>Amount of the Grant Allocated (Expressed in SDR Equivalent)</u>	<u>% of Expenditures to be Financed</u>
(1) Goods	733,000	0	100% of foreign expenditures and 90% of local expenditures
(2) Consultants' services including Audit	13,930,430	0	90%
(3) Training and Workshops	2,932,700	0	90%
(4) Operating Costs	2,200,000	0	90%
(5) Grants for Sub-projects (under Part B)	0	55,000,00	100% of the amounts disbursed
(6) Grants for Sub-projects (under Part C)	8,651,530	0	100% of the amounts disbursed
(7) Unallocated	8,252,340	0	
TOTAL	<u>36,700,000</u>	<u>55,000,000</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 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 for goods or services supplied from the territory of the Borrower;

(c) the term “Operating Costs” means the incremental operating costs arising under Parts A, D and E of the Project on account of Project implementation, management and monitoring, including office rent, equipment and office supplies, utilities, consumables, maintenance and operation of Project motor vehicles, travel and accommodation for Project staff, and salaries of support staff of the Project, excluding salaries of officials of the Borrower’s civil service; and

(d) the term “Training and Workshops” mean costs arising under Parts A, D and E of the Project on account of purchase of training materials and rental of training facilities, and includes workshops designated for the purpose of annual review for decentralization, mid-term review, best practice manuals, property data and assessment, property tax administration, Local Government enhancement help desk manual, and other workshops designed for the purpose of approved training.

3. Notwithstanding the provisions of paragraph 1 above, no withdrawals shall be made in respect of:

(a) payments made for expenditures prior to the date of this Agreement; and

(b) expenditures under Categories (5) and (6) unless the Eligible Local Governments have complied with the criteria, procedures and terms and conditions set forth or referred to in paragraphs 7 and 8 of Schedule 4 to this Agreement.

4. The Borrower has requested and the Association has agreed that withdrawals from the Credit Account or the Grant Account in respect of the Project be made on the basis of reports to be submitted by the Borrower 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 Disbursement). In the case of the first such request submitted to the Association before any withdrawal has been made from the Credit Account or the Grant 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.

5. The Association may require withdrawals from the Credit Account or the Grant Account to be made on the basis of statements of expenditure for expenditures under contracts for: (a) goods costing less than \$500,000 equivalent per contract; (b) for works, under contracts costing less than \$50,000, equivalent per contract; (c) for services of individual consultants costing less than \$100,000 equivalent per contract; and (d) for services of consulting firms under contracts costing less than \$350,000 equivalent per contract, all under such terms and conditions as the Association shall specify by notice to the Borrower.

B. Special Account

1. Upon receipt of notification from the Association allowing the establishment of the Special Accounts, the Borrower may open and maintain in Dollars in a commercial bank acceptable to the Association: (a) a special deposit account (Special Account “A”) for purposes of depositing the corresponding proceeds of the Financing for Parts A, D and E of the Project; and (b) a special deposit account (Special Account “B”) for the purposes of depositing the corresponding proceeds of the Financing for Parts B and C of the Project, both 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 Accounts have been opened, withdrawals from the Credit Account or the Grant account of amounts to be deposited into the respective Special Accounts 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 respective Special Accounts shall be made exclusively for Eligible Expenditures. For each payment made by the Borrower out of the respective 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 any 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 Sections 4.01 (b) (ii) and 4.02 (b) (ii) of this Agreement, any of the audit reports required to be furnished to the Association pursuant to said Sections in respect of the audit of: (i) the records and accounts for the respective Special Accounts; or (ii) the records and accounts reflecting expenditures with respect to which withdrawals were Report-based Disbursements or were made on the basis of statements of expenditure, as the case may be.

5. The Association shall not be required to make further deposits into any 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 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 respective Special Account may be made and what procedures should be followed for making such deposits, and shall notify the Borrower of its determination.

6. (a) If the Association determines at any time that any payment out of any 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 respective 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 any 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 a 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 or the Grant Account for subsequent withdrawal or for cancellation in accordance with the provisions of this Agreements, including the General Conditions.

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: (a) in respect of Special Account A an amount of \$460,000, to be withdrawn from the Credit Account and deposited into the Special Account pursuant to paragraph 2 of this Annex; and (b) in respect of Special Account B an amount of \$680,000, to be withdrawn from the Credit Account or the Grant 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 Accounts 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 A or B, as the case may be, of an amount or amounts which in the aggregate do not exceed the respective Authorized Allocation for Special Account A or B, as the case may be. On the basis of each such request or requests, the Association shall, on behalf of the Borrower, withdraw from the Credit Account or the Grant Account and deposit into the requested Special Account such amount or amounts as the Borrower shall have requested.

(b) For replenishment of the respective Special Account, the Borrower shall furnish to the Association requests for deposit into the respective 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.5 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 or the Grant Account and deposit into the requested 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 respective Special Account for Eligible Expenditures. Each such deposit into the respective Special Account shall be withdrawn by the Association from the Credit Account or the Grant Account under one or more of the Eligible Categories.

3. The Association shall not be required to make further deposits into any Special Account, once the total unwithdrawn amount of the Credit or the Grant 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 or the Grant Account of the remaining unwithdrawn amount of the Credit or the Grant 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 respective 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 or the Grant Account shall be deposited by the Association into the respective Special Account in accordance with the provisions of Schedule 1 to this Agreement. Each such deposit into any Special Account shall be withdrawn by the Association from the Credit Account or the Grant Account under one or more of the Eligible Categories.

2. Upon receipt of each application for withdrawal of an amount of the Credit or the Grant, the Association shall, on behalf of the Borrower, withdraw from the Credit Account or the Grant Account and deposit into the respective 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 assist the Borrower in improving the Local Government institutional performance for sustainable, decentralized service delivery.

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: Support to the Decentralization Process

1. Improving the Local Governments' capacity to implement the Fiscal Decentralization Strategy and tools to support decentralization of the development budget, including: (a) implementation of effective integrated budgeting planning systems; (b) strengthening the Local Governments' procurement systems; (c) dissemination and implementation of the Local Government Communication Strategy; and (d) implementation of a unified system for monitoring and evaluating performance, capacity and service delivery at the district and municipal council levels, all through the acquisition of goods and provision of technical advisory services.

2. Formulation of a strategy to improve local financial management in the Local Governments which are not covered by the integrated financial management system in the short to medium term.

3. (a) Supporting the institutional structure for decentralization by improving the capacity of Local Governments in administration, and ensuring coordinated structure for decentralization and performance assessment systems for Local Governments, through the acquisition of goods and provision of technical advisory service.

(b) Developing a national capacity building strategic framework and strengthening human resource development function of the Local Governments, through the provision of technical advisory services.

(c) Designing institutional arrangements and scope for future decentralization and modalities for donor support.

(d) Identifying contradictory or inconsistent policies, laws and practices within the framework for decentralization with a view to making recommendations for harmonization.

(e) Developing and implementing a framework for Local Governments' capacity building strategy for coordination of capacity building activities to support decentralization.

(f) Strengthening the capacity of the human resource development function of the Local Governments at the district and municipal council levels.

(g) Carrying out audits of all the Lower-Level Local Governments.

(h) Supporting the process of harmonization of procurement regulations and practices of the Local Governments and the central government, through the provision of technical advisory services and training.

Part B: Local Development Service Delivery

Strengthening the capacity of Eligible Local Governments in planning, implementation and sustainable service delivery in compliance with mandatory legal provisions, through the provision of Local Development Grants for implementation of Subprojects for local infrastructure and investment.

Part C: Local Government Capacity Building

Strengthening the capacity of Local Governments to implement the decentralization mandate, including enhancing the quality of training and establishment of a system to empower the Local Governments in defining their needs, procure and carry out training, through the provision of Capacity Building Grants.

Part D: Local Government Revenue Enhancement

Strengthening the capacity of Local Governments in administration of their sources of revenue, including: (a) supporting MOLG in improvement of the policy and legal framework relating to revenue sources and reviewing the structure for graduated tax, property tax and business levies and fees; (b) provision of training to political leaders and senior officials at the central and Local Government levels; (c) carrying out of a comprehensive study aimed at identifying best practice for local revenue enhancement; (d) carrying out of the introduction and improvement of the property tax system,

improvement of local government tax administration system, including: (i) property data collection and assessment; (ii) development of a comprehensive property tax administration system; and (iii) provision of training to educate, sensitize and ensure compliance with the requirements of the Local Governments (Rating) Act, upon its enactment; and (e) monitoring revenues, including: (i) finalization and adjustment of the Local Governments' financial information and analysis system; and (ii) data collection, reporting, verification and analysis, all through the provision of technical advisory services.

Part E: Project Management and Coordination

Strengthening of PCU's and MOLG's capacity in: (a) coordination and management of the Project including, *inter alia*, support in contract management, workshops and seminars; (b) implementation, monitoring and evaluation of the Project including, monitoring of any performance indicators and impact assessment, and workshop for final evaluation of the Project; and (c) audit of the accounts of the Project, all through the provision of technical advisory services.

* * *

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

SCHEDULE 3

Procurement

Section I. Procurement of Goods and Works

Part A: General

Goods and works shall be procured in accordance with the provisions of Section I of the “Guidelines for Procurement under IBRD Loans and IDA Credits” published by the Bank in January 1995 and revised in January and August 1996, September 1997 and January 1999 (the Guidelines) and the following provisions of this Section.

Part B: International Competitive Bidding

1. Except as otherwise provided in Part C of this Section, goods and works shall be procured under contracts awarded in accordance with the provisions of Section II of the Guidelines and paragraph 5 of Appendix 1 thereto.
2. The following provisions shall apply to goods and works to be procured under contracts awarded in accordance with the provisions of paragraph 1 of this Part B.

Notification and Advertising

The invitation to prequalify or bid for each contract estimated to cost \$500,000 equivalent or more shall be advertised in accordance with the procedures applicable to large contracts under paragraph 2.8 of the Guidelines.

Part C: Other Procurement Procedures

1. National Competitive Bidding

(a) Goods estimated to cost less than \$ 500,000 equivalent per contract, may be procured under contracts awarded in accordance with the provisions of paragraphs 3.3 and 3.4 of the Guidelines.

(b) Works: (i) for Kampala City Council, estimated to cost more than \$100,000 equivalent per contract; and (ii) for all other Eligible Local Governments, estimated to cost more than \$50,000 equivalent per contract, may be procured under

contracts awarded in accordance with the provisions of paragraphs 3.3 and 3.4 of the Guidelines.

2. Shopping

Goods estimated to cost less than \$30,000 equivalent per contract, may be procured under contracts awarded on the basis of shopping procedures in accordance with the provisions of paragraphs 3.5 and 3.6 of the Guidelines.

3. Procurement of Small Works

Works: (a) for Kampala City Council, estimated to cost less than \$100,000 equivalent per contract; and (b) for all other Eligible Local Governments, estimated to cost less than \$50,000 equivalent per contract, may be procured under lump-sum, fixed-price contracts awarded on the basis of quotations obtained from three (3) qualified domestic contractors in response to a written invitation. The invitation shall include a detailed description of the works, including basic specifications, the required completion date, a basic form of agreement acceptable to the Association, and relevant drawings, where applicable. The award shall be made to the contractor who offers the lowest price quotation for the required work, and who has the experience and resources to complete the contract successfully.

Part D: Review by the Association of Procurement Decisions

1. Procurement Planning

Prior to the issuance of any invitations to bid for contracts, the proposed procurement plan for the Project shall be furnished to the Association for its review and approval, in accordance with the provisions of paragraph 1 of Appendix 1 to the Guidelines. Procurement of all goods and works shall be undertaken in accordance with such procurement plan as shall have been approved by the Association, and with the provisions of said paragraph 1.

2. Prior Review

(a) With respect to each contract for goods estimated to cost the equivalent of \$500,000 or more, the procedures set forth in paragraphs 2 and 3 of Appendix 1 to the Guidelines shall apply.

(b) Each contract for works: (i) for Kampala City Council, estimated to cost the equivalent of \$100,000 or more; and (ii) for all other Eligible Local Governments, estimated to cost the equivalent of \$ 50,000 or more, shall be subject to prior review by the MOLG following the Borrower's procurement procedures.

3. Post Review

With respect to each contract not governed by paragraph 2 of this Part, the procedures set forth in paragraph 4 of Appendix 1 to the Guidelines shall apply.

Section II. Employment of Consultants

Part A: General

Consultants' services shall be procured in accordance with the provisions of Sections I and IV of the "Guidelines: Selection and Employment of Consultants by World Bank Borrowers" published by the Bank in January 1997 and revised in September 1997, January 1999 and May 2002 (the Consultant Guidelines), paragraph 1 of Appendix 1 thereto, Appendix 2 thereto and the following provisions of Section II of this Section.

Part B: Quality- and Cost-based Selection

1. Except as otherwise provided in Part C of this Section, consultants' services shall be procured under contracts awarded in accordance with the provisions of Section II of the Consultant Guidelines, and the provisions of paragraphs 3.13 through 3.18 thereof applicable to quality- and cost-based selection of consultants.

2. The following provision shall apply to consultants' services to be procured under contracts awarded in accordance with the provisions of the preceding paragraph: the short list of consultants for services, estimated to cost less than \$200,000 equivalent per contract, may comprise entirely national consultants in accordance with the provisions of paragraph 2.7 and footnote 8 of the Consultant Guidelines.

Part C: Other Procedures for the Selection of Consultants

1. Quality-based Selection

Services for training institutions for workshops and training shall be procured under contracts awarded in accordance with the provisions of paragraphs 3.1 through 3.4 of the Consultant Guidelines.

2. Least-cost Selection

Services for financial audits and other contracts of a routine nature where well established practices and standards exist, estimated to cost less than \$200,000 equivalent per contract may be procured under contracts awarded in accordance with the provisions of paragraphs 3.1 and 3.6 of the Consultant Guidelines.

3. Selection Based on Consultants' Qualifications

Services estimated to cost less than \$100,000 equivalent per contract may be procured under contracts awarded in accordance with the provisions of paragraphs 3.1 and 3.7 of the Consultant Guidelines.

4. Single Source Selection

In exceptional cases, where the overall interests of the client and the Project demand, selection of consultants may, with the Association's prior agreement, be procured in accordance with the provisions of paragraphs 3.8 through 3.11 of the Consultant Guidelines.

5. Individual Consultants

Services of individual consultants for tasks that meet the requirements set forth in paragraph 5.1 of the Consultant Guidelines shall be procured under contracts awarded in accordance with the provisions of paragraphs 5.1 through 5.3 of the Consultant Guidelines.

Part D: Review by the Association of the Selection of Consultants

1. Selection Planning

A plan for the selection of consultants, which shall include contract cost estimates, contract packaging, and applicable selection criteria and procedures, shall be furnished to the Association for its review and approval prior to the issuance to consultants of any requests for proposals. Selection of all consultants' services shall be undertaken in accordance with such selection plan as updated from time to time as shall have been approved by the Association.

2. Prior Review

(a) With respect to each contract for the employment of consulting firms estimated to cost the equivalent of \$350,000 or more, the procedures set forth in paragraphs 2, 3 and 5 of Appendix 1 to the Consultant Guidelines shall apply.

(b) With respect to each contract for the employment of individual consultants estimated to cost the equivalent of \$100,000 or more, the report on the comparison of the qualifications and experience of candidates, the qualifications, experience, terms of reference and terms of employment of the consultants shall be furnished to the Association for its prior review and approval. The contract shall be awarded only after the said approval shall have been given. The provisions of paragraph 3 of Appendix 1 to the Consultant Guidelines shall also apply to such contracts.

(c) All single source selection for contracts estimated to cost more than \$5,000 shall be subject to prior review by the Association.

3. Post Review

With respect to each contract not governed by paragraph 2 of this Part, the procedures set forth in paragraph 4 of Appendix 1 to the Consultant Guidelines shall apply.

SCHEDULE 4

Implementation Program

Part A: Overall Project Implementation

1. The MOLG shall be responsible for execution, coordination and management of the Project with the technical support of its PCU. To this end, MOLG shall maintain the PCU with staffing, terms of reference and functions satisfactory to the Association.

2. The Borrower shall:

 (a) implement the Project in accordance with the Project Implementation Plan in form and substance acceptable to the Association giving details of all procurement and disbursement arrangements, performance indicators and other administrative, financial and organizational arrangements, as shall have been agreed with the Association for the purposes of the Project; and

 (b) carry out the Project in accordance with procedures set out in the Project Implementation Plan, and, except as the Association may otherwise agree, shall not amend or waive any provision thereof, if such amendment or waiver may, in the opinion of the Association, materially or adversely affect the implementation of the Project.

3. The Borrower shall, not later than December 31, 2003, update the chart of accounts for the Project, in a form and substance satisfactory to the Association, for the purpose of accounting for activities under the Project.

Part B: Terms and Conditions for Financing of Subprojects Under Parts B and C of the Project

4. Pursuant to the provisions of paragraph 6 of this Schedule, any Subproject under Part B of the Project shall be:

 (a) initiated by an Eligible Local Government and identified as an infrastructure investment activity, acceptable to the Association, under functions of a Higher-Level Local Government or a Lower-Level Local Government pursuant to Parts 2 through 5 of the Second Schedule to the Local Governments Act;

 (b) appraised and carried out in accordance with the procedures and conditions set forth in the Project Implementation Plan;

(c) economically and technically viable in accordance with the standards specified in the Project Implementation Plan; and

(d) in compliance with the standards set forth in the applicable laws and regulations of the Borrower relating to health, safety and environmental management.

5. To be eligible for financing to implement a Subprojects under Parts B and C of the Project an Eligible Local Government shall satisfy the eligibility criteria specified in the Project Implementation Plan.

6. Participation Agreement:

For the purposes of Parts B and C of the Project, the Borrower shall conclude an agreement (hereinafter called a Participation Agreement) with each Higher Level Local Government, whereby the Borrower shall agree to provide to such Higher Level Local Government a grant, on a non-reimbursable basis, and on terms and conditions set forth in this paragraph 6, including details of disbursement schedules and procurement procedures, the amount of the Higher Level Local Government's counterpart contribution, details of any further safeguards as may be needed for the management of the environment, and the following additional terms and Conditions:

(a) require the Higher Level Local Government to carry out any Subproject under Parts B and C of the Project with due diligence and efficiency and in accordance with sound technical, financial, managerial and environmental standards and practices, and maintain adequate records;

(b) obtain all such information as the Association or the Higher Level Local Government shall reasonably request relating to the implementation of a Subproject under Parts B and C of the Project, and the performance of the Higher Level Local Government thereunder; and

(c) suspend or terminate the right of an Higher Level Local Government to the use of the proceeds of the Financing upon failure by such Higher Level Local Government to perform its obligations under the Participation Agreement.

7. Proceeds of the Financing allocated under Category (5) in the table set forth under paragraph 1 of Schedule 1 to this Agreement, shall be disbursed on a quarterly basis in three yearly installments, provided that the Borrower has furnished to the Association:

- (a) for the first year:
 - (i) certification indicating that there have been no: (A) significant reallocations, deviations; or (B) suspension or partial suspension of LGDP1 Third Tranche funds as compared to the indicative planning figures for the Local Governments;
 - (ii) a schedule, in form and substance satisfactory to the Association, indicating the amounts of Local Development Grants released to Eligible Local Governments during the preceding Fiscal Year;
 - (iii) initial cashflow forecasts for Local Development Grants based on the results of the annual assessment;
 - (iv) the Participation Agreements referred to in paragraph 6 of this Schedule;
 - (v) a document outlining the process for creation of new Districts in accordance with the Borrower's laws; and
 - (vi) an audit strategy for the Lower Local Governments prepared by the Borrower's Auditor General.

- (b) for the second year:
 - (i) a financial performance assessment report with respect to expenditures for Local Development Grants, in form and substance satisfactory to the Association, carried out by MOLG in the preceding Fiscal Year;
 - (ii) a schedule indicating the funds released by the Borrower to the Local Governments through Local Development Grants during the previous Fiscal Year, and amounts to be released in the in the following Fiscal Year;
 - (iii) certification indicating that there have been no: (A) significant reallocations, deviations; or (B) suspension of Financing in the first year, as compared to the indicative planning figures for the Local Governments;

- (iv) Participation Agreements referred to in paragraph 6 of this Schedule in respect of any Eligible Local Government participating for the first time;
 - (v) submission of a Local Governments (Rating) Bill, in form and substance satisfactory to the Association;
 - (vi) progress report on implementation of the Institutional Plan, in form and substance satisfactory to the Association; and
 - (vii) progress report on implementation of the audit strategy for the Lower-Level Local Governments, in form and substance satisfactory to the Association.
- (c) for the third year:
- (i) a financial performance assessment report with respect to expenditures for Local Development Grants, in form and substance satisfactory to the Association, carried out by MOLG in the preceding Financial Year;
 - (ii) a schedule indicating the funds released by the Borrower to the Local Governments through Local Development Grants during the previous Fiscal Year, and amounts to be released in the following Fiscal Year;
 - (iii) certification indicating that there have been no: (A) significant reallocations, deviations; or (B) suspension of Financing in the second year as compared to the indicative planning figures for the Local Governments;
 - (iv) Participation Agreements referred to under paragraph 6 of this Schedule in respect of any Eligible Local Government participating for the first time;
 - (v) submission of a Local Governments (Rating) Act, referred to in paragraph 15 of the Letter of Sector Policy, including, mass valuation regulations; and

- (vi) a report, satisfactory to the Association, on an independent procurement review carried out in all the Higher-Level Local Governments.

8. Proceeds of the Financing allocated under Category (6) in the table set forth under paragraph 1 of Schedule 1 to this Agreement, shall be disbursed on a quarterly basis in four yearly installments, provided that the Borrower shall in each year have furnished to the Association:

- (a) Participation Agreements referred to in paragraph 6 of this Schedule; and
- (b) record of accounts, satisfactory to the Association indicating the funds released by the Borrower to the Local Governments through the Capacity Building Grants during the preceding accounting period.

Part C: Environmental and Social Management Framework and Resettlement Policy Framework

9. The Borrower shall cause Eligible Local Governments:

- (a) prior to commencing any Subproject and when required under the Environmental and Social Management Framework, carry out an environmental impact assessment in accordance with the Environmental Checklist, and in a form satisfactory to the Association;
- (b) in the event that an environmental and social impact assessment of a Subproject determines that such a Subproject, if carried out, would have in the opinion of the Association a potential for negative environmental impact, not approve such a Subproject until an appropriate action has been discussed and agreed upon by the Borrower and the Association to mitigate such potential negative impact; and
- (c) thereafter cause the relevant Local Government to carry out such agreed mitigation plan referred to in sub-paragraph (b) above.

10. Prior to commencement of a Subproject involving involuntary resettlement or involuntary acquisition of land, the Borrower shall cause Eligible Local Governments to prepare and implement appropriate resettlement plans for compensation, resettlement and rehabilitation, in accordance with the Resettlement Policy Framework, and in form and substance satisfactory to the Association.

Part D: Monitoring and Reporting

11. The Borrower shall:

(a) maintain policies and procedures adequate to enable it to monitor and evaluate on an ongoing basis, in accordance with the indicators set forth in Schedule 5 to this Agreement, the carrying out of the Project and the achievement of the objectives thereof;

(b) prepare, under terms of reference satisfactory to the Association, and furnish to the Association, on or about October 31 of each year, a report integrating the results of the monitoring and evaluation activities performed pursuant to paragraph (a) of this Section, on the progress achieved in the carrying out of the Project during the period preceding the date of said report and setting out the measures recommended to ensure the efficient carrying out of the Project and the achievement of the objectives thereof during the period following such date;

(c) prepare under terms of reference satisfactory to the Association, and furnish to the Association, on or about August 15 and February 15, a bi-annual report, which shall cover salient aspects of the Project, including progress in the achievement of the objectives of the Project; and

(d) review with the Association, by December 31 of each year, or such later date as the Association shall request, the report referred to in paragraph (b) of this Section, and thereafter act promptly and diligently in order to take, any corrective action deemed necessary to remedy any shortcoming identified in the implementation of the Project, or to implement such measures as may have been agreed between the Borrower and the Association in furtherance of the objectives of the Project.

12. Midterm Review

(a) The Borrower shall not later than February 15, 2005, carry out jointly with the Association a midterm review, which shall cover among other things: (i) the performance by Local Governments under Parts B and C of the Project; (ii) progress in meeting the Project's objectives; and (iii) overall Project performance as measured against the performance indicators referred to in paragraph 11 (a) of this Schedule 4.

(b) Thereafter, take all measures required to ensure the efficient completion of the Project and the achievement of the objectives thereof, based on the conclusions and recommendations of the said report and the Association's views on the matter.

SCHEDULE 5

Monitoring Indicators

1. 75% of Local Governments with a three year rolling Development Plan.
2. 75% of High Level Local Governments submitted final accounts on time to the Office of the Auditor General.
3. 35% of Local Governments registering 20% increase in own revenue (taxes, user charges and fees) from baseline year 2002/2003.

SCHEDULE 6

Modifications to the General Conditions

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

1. Section 1.01 is amended to read:

“These General Conditions set forth certain terms and conditions generally applicable to development financing granted by the Association as a development credit and development grant to its members. They apply to any development financing agreement providing for any such development finance to the extent and subject to any modifications set forth in such agreement.

2. Paragraph 8 of Section 2.01 is amended to read as follows:

8. “Development Financing Agreement” means the particular Development Financing Agreement to which these General Conditions apply, as such agreement may be amended from time to time. Development Financing Agreement includes these General Conditions as applied thereto, and all schedules and agreements supplemental to the Development Financing Agreement

3. The following new paragraphs are added to Section 2.01:

15. “Grant” means the development grant provided for in the Development Financing Agreement.”;

16. “Grant Account” means the account opened by the Association on its books in the name of the Borrower to which the amount of the Grant is credited.”;

17. “Financing” means, collectively, the Credit and the Grant.

18. “Financing Accounts” means, collectively, the Credit Account and the Grant Account (or, where the context so requires, either of the Credit Account or the Grant Account).

4. The term “Credit”, wherever used in the following Articles and Sections of the General Conditions, is amended to read “Financing”: Sections 2.01(3), 2.01(12), 4.01, Article V, Article VI (excluding Section 6.05), Section 7.01(d), Article VIII, and Article IX.

5. The term “Credit Account”, wherever used in the following Articles and Sections of the General Conditions, is amended to read “Financing Accounts”: Section 2.01(6), 4.01, Article V, Article VI, and Section 12.03.

6. The term “Development Credit Agreement”, wherever used in the General Conditions, is amended to read the Development Financing Agreement.

7. Section 3.01 is modified to read as follows:

“Section 3.01. *Financing Accounts.* The amount of the Credit shall be credited to the Credit Account and may be withdrawn from the Credit Account by the Borrower as provided in the Development Financing Agreement and in these General Conditions. The amount of the Grant shall be credited to the Grant Account and may be withdrawn from the Grant Account by the Borrower as provided in the Development Financing Agreement and in these General Conditions.”

8. The phrase “(including any development financing agreement or development grant agreement)” is added to Section 6.02(a)(ii) after the words “any development credit agreement” and before the words “between the Borrower and the Association”, to Section 6.02(c)(i) after the words “any development credit agreement” and before the words “with the Association”, and to Section 7.01(b)(i) after the words “any other development credit agreement” and before the words “between the Borrower and the Association”:

9. Section 6.05 is amended to read as follows:

“Except as the Borrower and the Association shall otherwise agree, any cancellation of any amount of the Credit shall be applied *pro rata* to the several installments of the principal amount of the Credit maturing after the date of such cancellation.”

