

Public Disclosure Authorized

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LOAN NUMBER 7202-CH

Loan Agreement

(Social Protection Sector Adjustment Loan)

between

REPUBLIC OF CHILE

and

**INTERNATIONAL BANK FOR RECONSTRUCTION
AND DEVELOPMENT**

Dated January 6, 2004

Public Disclosure Authorized

LOAN NUMBER 7202-CH

LOAN AGREEMENT

AGREEMENT, dated January 6, 2004, between REPUBLIC OF CHILE (the Borrower) and INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT (the Bank).

WHEREAS (A) the Bank has received from the Borrower a letter, dated October 19, 2003, describing a program of actions, objectives and policies designed to achieve structural adjustment of the Borrower's social protection system (hereinafter called the Program), declaring the Borrower's commitment to the execution of the Program, and requesting assistance from the Bank in support of the Program during the execution thereof;

WHEREAS (B) the Borrower has carried out the measures and taken the actions described in Schedule 2 to this Agreement (the Program) to the satisfaction of the Bank and has maintained a macroeconomic policy framework satisfactory to the Bank;

WHEREAS (C) the Borrower may elect to withdraw the proceeds of the Loan provided for in Article II of this Agreement at any time within three years from the date of this Agreement (or any longer period that the Bank may establish as provided in Section 2.03 of this Agreement) when a financing need arises, subject to the provision of Section 2.02 (c) of this Agreement; and

WHEREAS (D) on the basis, *inter alia*, of the foregoing, the Bank has decided in support of the Program to provide such assistance to the Borrower by making the Loan in one tranche as hereinafter provided;

NOW THEREFORE the parties hereto hereby agree as follows:

ARTICLE I

General Conditions; Definitions

Section 1.01. The "General Conditions Applicable to Loan and Guarantee Agreements for Fixed Spread Loans" of the Bank, dated September 1, 1999, with the modifications thereto set forth below (the General Conditions) constitute an integral part of this Agreement:

- (a) Section 2.01, paragraph 41, is modified to read:

“‘Project’ means the program, referred to in the Preamble to the Loan Agreement, in support of which the Loan is made”;

- (b) Section 3.08 is modified to read:

“Each withdrawal of an amount from the Loan Account shall be made in the Loan Currency of such amount. The Bank, at the request and acting as an agent of the Borrower, shall purchase with the Loan Currency withdrawn from the Loan Account the currency or currencies of the deposit account specified in Section 2.02 of the Loan Agreement.”;

- (c) Section 5.01 is modified to read:

“The Borrower shall be entitled to withdraw the proceeds of the Loan from the Loan Account in accordance with the provisions of the Loan Agreement and of these General Conditions”;

- (d) The last sentence of Section 5.03 is deleted;

- (e) Section 9.07 (c) shall be modified to read:

“(c) 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 Bank, the Borrower shall prepare and furnish to the Bank a report, of such scope and in such detail as the Bank shall reasonably request, on the execution of the program referred to in the Preamble to the Loan Agreement, the performance by the Borrower and the Bank of their respective obligations under the Loan Agreement and the accomplishment of the purposes of the Loan.”; and

- (f) Section 9.05 is deleted and Sections 9.06, 9.07 (as modified above), 9.08 and 9.09 are renumbered, respectively, Sections 9.05, 9.06, 9.07 and 9.08.

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) “Advisory Committee” means the committee established by Decree No. 144 for the initial implementation of Chile *Solidario* and composed of, *inter alia*, MIDEPLAN, FOSIS and the Borrower’s Ministries of Finance and Labor;

(b) “Chilean Peso” means the Borrower’s currency;

(c) “Chile *Solidario*” means the social protection system referred to in Decree No. 144;

(d) “Chile *Solidario* Financing Legislation” means Law No. 19888 published in the Official Gazette on August 13, 2003 for the financing of priority social programs including Chile *Solidario*;

(e) “Decree No. 144” means the Borrower’s Presidential Decree published in the Official Gazette on August 19, 2002 regarding the establishment of the Advisory Committee;

(f) “Deposit Account” means the account referred to in Section 2.02 (b) of this Agreement;

(g) “Disbursed Amount” means, in respect of each Interest Period, the aggregate principal amount of the Loan withdrawn from the Loan Account in said Interest Period;

(h) “*Ficha CAS*” means the Borrower’s targeting instrument used to prioritize recipients of social transfers referred to in MIDEPLAN’s document entitled “*Mejoramiento del Factor Discriminatorio de la FICHA CAS*”, dated December 2002;

(i) “FOSIS” means the Borrower’s social investment fund established pursuant to Law No. 18989 published in the Official Gazette on July 19, 1990;

(j) “Maturity Fixing Date” means, for each Disbursed Amount, the date on which the amortization schedule for said Disbursed Amount is established, such date being the first day of the Interest Period next following the Interest Period in which said Disbursed Amount is withdrawn;

(k) “MIDEPLAN” means the Borrower’s Ministry of Planning and Cooperation;

(l) “National Social Protection Information System” means the system described in Section 2 of the Borrower’s document entitled “*Proyecto Integración Asistencia Técnica Chile Solidario – Banco Mundial*”, dated September 2003;

(m) “Official Gazette” means the Borrower’s *Diario Oficial*;

(n) “PASIS” means *Pensiones Asistenciales*, the Borrower’s program of non-contributory social assistance benefits for elderly and disabled indigents set forth in Decree-Law No. 869 of January 28, 1975; and

(o) “SUF” means *Subsidio Unico Familiar*, the Borrower’s program of non-contributory single subsidy for poor families set forth in Law No. 18020 published in the Official Gazette on August 17, 1981.

ARTICLE II

The Loan

Section 2.01. The Bank agrees to lend to the Borrower, on the terms and conditions set forth or referred to in the Loan Agreement, an amount equal to two hundred million Dollars (\$200,000,000) as such amount may be converted from time to time through a Currency Conversion in accordance with the provisions of Section 2.09 of this Agreement.

Section 2.02. (a) Subject to the provisions of paragraphs (b), (c) and (d) of this Section, the Borrower shall be entitled to withdraw the proceeds of the Loan from the Loan Account in up to three draw-downs in support of the Program.

(b) The Borrower shall open, prior to furnishing to the Bank the first request for withdrawal from the Loan Account, and thereafter maintain in its Central Bank, a deposit account in Dollars on terms and conditions satisfactory to the Bank. Withdrawals from the Loan Account, except those for the payment of the front-end fee set forth in Section 2.04 of this Agreement, shall be deposited by the Bank into the Deposit Account.

(c) The Borrower shall be entitled to withdraw any amount from the Loan Account for deposit in the Deposit Account only after the Bank shall be satisfied, after an exchange of views as described in Section 3.01 of this Agreement, that: (i) the macroeconomic policy framework of the Borrower continues to be consistent with the objectives of the Program; and (ii) the Borrower continues to adhere to the Program and its actions and policies remain consistent with the objectives of the Program.

(d) The Borrower undertakes that the proceeds of the Loan shall not be used to finance expenditures excluded pursuant to the provisions of Schedule 1 to this Agreement. If the Bank shall have determined at any time that any proceeds of the Loan shall have been used to make a payment for an expenditure so excluded, the Borrower shall, promptly upon notice from the Bank; (i) deposit into the Deposit Account an amount equal to the amount of said payment; or (ii) if the Bank shall so request, refund such amount to the Bank. Amounts refunded to the Bank upon such request shall be credited to the Loan Account for cancellation.

Section 2.03. The Closing Date shall be January 6, 2007 or such later date as the Bank shall establish. The Bank shall promptly notify the Borrower of such later date.

Section 2.04. The Borrower shall pay to the Bank a fee in an amount equal to one percent (1%) of any amount withdrawn from the Loan Account. On the date of such withdrawal, the Bank shall: (a) retain one percent (1%) of the withdrawn amount for itself in payment of said fee; and (b) immediately thereafter deposit the remainder of the withdrawn amount into the Deposit Account.

Section 2.05. The Borrower shall pay to the Bank a commitment charge at the rate of one percent (1%) per annum on the unwithdrawn principal amount.

Section 2.06. The Borrower shall pay interest on the principal amount of the Loan withdrawn and outstanding from time to time, in respect of each Interest Period at the Variable Rate; provided, that upon a Conversion of all or any portion of the principal amount of the Loan, the Borrower shall, during the Conversion Period, pay interest on such amount in accordance with the relevant provisions of Article IV of the General Conditions.

Section 2.07. Interest and other charges shall be payable semiannually in arrears on June 15 and December 15 in each year.

Section 2.08. (a) Subject to the provisions of paragraph (b) of this Section, the Borrower shall repay each Disbursed Amount in full on the ninth (9th) Interest Payment Date following the Maturity Fixing Date for said Disbursed Amount.

(b) Notwithstanding the provisions of paragraph (a) of this Section, if any Disbursed Amount would, pursuant to the provisions of such paragraph (a), be payable after June 15, 2008, the Borrower shall also pay on such date the aggregate amount of all such Disbursed Amounts.

(c) The Bank shall notify the Borrower of the Principal Payment Date for each Disbursed Amount promptly after the Maturity Fixing Date for said Disbursed Amount.

(d) Notwithstanding the provisions of paragraph (a) through (c) of this Section, in the event of a Currency Conversion of all or any portion of a Disbursed Amount to an Approved Currency, the amount so converted in said Approved Currency that shall be repayable on any Principal Payment Date occurring during the Conversion Period, shall be determined by the Bank by multiplying such amount in its currency of denomination immediately prior to said Conversion by either: (i) the exchange rate that reflects the amounts of principal in said Approved Currency payable by the Bank under the Currency Hedge Transaction relating to said Conversion; or (ii) if the Bank so determined in accordance with the Conversion Guidelines, the exchange rate component of the Screen Rate.

Section 2.09. (a) The Borrower may at any time request any of the following Conversions of the terms of the Loan in order to facilitate prudent debt management:

- (i) a change of the Loan Currency of all or any portion of the principal amount of the Loan, withdrawn or unwithdrawn, to an Approved Currency;
- (ii) a change of the interest rate basis applicable to all or any portion of the principal amount of the Loan from a Variable Rate to a Fixed Rate, or vice versa; and
- (iii) the setting of limits on the Variable Rate applicable to all or any portion of the principal amount of the Loan withdrawn and outstanding by the establishment of an Interest Rate Cap or Interest Rate Collar on said Variable Rate.

(b) Any conversion requested pursuant to paragraph (a) of this Section that is accepted by the Bank shall be considered a "Conversion", as defined in Section 2.01(7) of the General Conditions, and shall be effected in accordance with the provisions of Article IV of the General Conditions and of the Conversion Guidelines.

ARTICLE III

Particular Covenants

Section 3.01. (a) The Borrower undertakes to implement the Program with due diligence to ensure that actions and policies adopted under the Program are put into effect.

(b) The Borrower and the Bank shall from time to time, at the request of either party, exchange views on the consistency of the Borrower's macroeconomic framework with the objectives of the Program, and the continued adherence of the Borrower to the Program.

(c) The Borrower and the Bank shall from time to time, at the request of either party, exchange views on the progress achieved in carrying out the Program.

(d) Prior to each such exchange of views, the Borrower shall furnish to the Bank for its review and comment a report on the progress achieved in carrying out the Program, in such detail as the Bank shall reasonably request.

(e) Without limitation upon the provisions of paragraph (b) of this Section, the Borrower shall exchange views with the Bank on any proposed action to be taken after the disbursement of the Loan which would have the effect of materially reversing the objectives of the Program, or any action taken under the Program, including any action specified in Schedule 2 to this Agreement.

Section 3.02. Upon the Bank's request, the Borrower shall:

(a) have the Deposit Account audited in accordance with appropriate auditing principles consistently applied, by independent auditors acceptable to the Bank;

(b) furnish to the Bank as soon as available, but in any case not later than four (4) months after the date of the Bank's request for such audit, a certified copy of the report of such audit by said auditors, of such scope and in such detail as the Bank shall have reasonably requested; and

(c) furnish to the Bank such other information concerning the Deposit Account and the audit thereof as the Bank shall have reasonably requested.

ARTICLE IV

Additional Event of Suspension

Section 4.01. Pursuant to Section 6.02 (p) of the General Conditions, the following additional event is specified, namely, that a situation has arisen which shall make it improbable that the Program, or a significant part thereof, will be carried out.

ARTICLE V

Effective Date; Termination

Section 5.01. The date April 5, 2004 is hereby specified for the purposes of Section 12.04 of the General Conditions.

ARTICLE VI

Representative of the Borrower; Addresses

Section 6.01. The Minister of Finance of the Borrower is designated as representative of the Borrower for the purposes of Section 11.03 of the General Conditions.

Section 6.02. The following addresses are specified for the purposes of Section 11.01 of the General Conditions:

For the Borrower:

Ministry of Finance
Teatinos 120
Santiago, Chile

Facsimile: (56-2) 698-8903

For the Bank:

International Bank for
Reconstruction and Development
1818 H Street, N.W.
Washington, D.C. 20433
United States of America

Cable address:

Telex:

Facsimile:

INTBAFRAD
Washington, D.C.

248423 (MCI) or
64145 (MCI)

(202) 477-6391

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

REPUBLIC OF CHILE

By /s/ Andrés Bianchi

Authorized Representative

INTERNATIONAL BANK FOR
RECONSTRUCTION AND DEVELOPMENT

By /s/ Daniela Gressani

Acting Regional Vice President
Latin America and the Caribbean

Countersigned on behalf of the
Treasurer General of the Republic of Chile

By: /s/ Andrés Bianchi
Authorized Representative

Countersigned on behalf of the
Controller General of the Republic of Chile

By: /s/ Andrés Bianchi
Authorized Representative

SCHEDULE 1

Excluded Expenditures

For purposes of Section 2.02 (d) of this Agreement, the proceeds of the Loan shall not be used to finance any of the following expenditures:

1. expenditures in the currency of the Borrower or for goods or services supplied from the territory of the Borrower;
2. expenditures for goods or services supplied under a contract which any national or international financing institution or agency other than the Bank or the Association shall have financed or agreed to finance, or which the Bank or the Association shall have financed or agreed to finance under another loan or a credit;
3. expenditures for goods included in the following groups or subgroups of the Standard International Trade Classification, Revision 3 (SITC, Rev.3), published by the United Nations in Statistical Papers, Series M, No. 34/Rev.3 (1986) (the SITC), or any successor groups or subgroups under future revisions to the SITC, as designated by the Bank by notice to the Borrower:

<u>Group</u>	<u>Subgroup</u>	<u>Description of Items</u>
112	-	Alcoholic beverages
121	-	Tobacco, unmanufactured, tobacco refuse
122	-	Tobacco, manufactured (whether or not containing tobacco substitutes)
525	-	Radioactive and associated materials
667	-	Pearls, precious and semiprecious stones, unworked or worked

718	718.7	Nuclear reactors, and parts thereof; fuel elements (cartridges), non-irradiated, for nuclear reactors
728	728.43	Tobacco processing machinery
897	897.3	Jewelry of gold, silver or platinum group metals (except watches and watch cases) and goldsmiths' or silversmiths' wares (including set gems)
971	-	Gold, non-monetary (excluding gold ores and concentrates)

4. expenditures for goods intended for a military or paramilitary purpose or for luxury consumption;

5. expenditures for environmentally hazardous goods (for purposes of this paragraph the term "environmentally hazardous goods" means goods, the manufacture, use or import of which is prohibited under the laws of the Borrower or international agreements to which the Borrower is a party);

6. expenditures: (a) in the territories of any country which is not a member of the Bank or for goods procured in, or services supplied from, such territories; or (b) on account of any payment to persons or entities, or any import of goods, if such payment or import is prohibited by a decision of the United Nations Security Council taken under Chapter VII of the Charter of the United Nations; and

7. expenditures under a contract in respect of which the Bank determines that corrupt or fraudulent practices were engaged in by representatives of the Borrower or of a beneficiary of the Loan during the procurement or execution of such contract, without the Borrower having taken timely and appropriate action satisfactory to the Bank to remedy the situation.

SCHEDULE 2

Actions Referred to in Recital (B) of the Preamble to this Agreement

A. Reforms of Poverty Reduction and Social Protection Policies

1. The Borrower has issued Decree No. 144 and created the Advisory Committee.
2. The Borrower has budgeted, in the proposed budget law for 2004, an amount of Chilean Pesos 40,864,000 for the financing during 2004 of Chile *Solidario*.
3. The Borrower has adopted the Chile *Solidario* Financing Legislation.
4. The Borrower has adopted Law No. 19873 published in the Official Gazette on May 25, 2003, creating a program of targeted school retention vouchers.
5. The Borrower, through MIDEPLAN, has signed agreements (*protocolos*) with at least 25 of its ministries and agencies for cooperation in the implementation of Chile *Solidario*.
6. The Borrower has submitted to its Congress a draft bill of Law (Draft No. 228-349 of September 1, 2003) for: (a) the operation of Chile *Solidario*; (b) the transferring of the administration, as part of Chile *Solidario*, of SUF and PASIS to MIDEPLAN; and (c) the establishment of a new cash transfer for participating beneficiaries of Chile *Solidario*.

B. National Information System for Social Protection

1. The Borrower, through MIDEPLAN, has completed an evaluation of the *Ficha* CAS, proposed measures to improve it, and piloted the new *Ficha* CAS in at least 15 municipalities.
2. The Borrower has included the National Social Protection Information System in the Borrower's electronic government initiative by instructions in the Borrower's letter dated October 1, 2003.
3. The Borrower has submitted to its Congress a draft bill of law (Draft No. 228-349 of September 1, 2003) for the establishment of a national information system for social protection.

C. Monitoring, Implementation and Impact Evaluation of Social Protection Programs

The Borrower has presented to the Bank a plan, satisfactory to the Bank, for evaluation of the impact of the implementation of Chile *Solidario* on the welfare of the participants.

D. Decentralized and Civil Society Roles in Social Assistance Programs

1. The Borrower, through FOSIS, has signed agreements with 332 municipalities for implementation of Chile *Solidario*.

2. The Borrower has adopted Law No. 19885, published in the Official Gazette on August 6, 2003, allowing tax deductions for private donations to civil society organizations working on alleviating and eradicating poverty.