

**CONFORMED COPY**

**CREDIT NUMBER 3941-HO  
SUPPLEMENTAL CREDIT NUMBER 3941-1-HO**

# **Development Credit Agreement**

**(Poverty Reduction Support Credit)**

**between**

**REPUBLIC OF HONDURAS**

**and**

**INTERNATIONAL DEVELOPMENT ASSOCIATION**

**Dated August 18, 2004**

**CREDIT NUMBER 3941-HO  
SUPPLEMENTAL CREDIT NUMBER 3941-1-HO**

**DEVELOPMENT CREDIT AGREEMENT**

AGREEMENT, dated August 18, 2004, between REPUBLIC OF HONDURAS (the Borrower) and INTERNATIONAL DEVELOPMENT ASSOCIATION (the Association).

WHEREAS (A) the Association has received from the Borrower a letter dated May 26, 2004, describing a program of actions, objectives and policies designed to achieve poverty reduction (hereinafter called the Program), declaring the Borrower's commitment to the execution of the Program, and requesting assistance from the Association 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 of this Agreement to the satisfaction of the Association and has maintained a macroeconomic policy framework satisfactory to the Association;

WHEREAS (C) the Borrower is eligible and meets the requirements to receive a supplemental credit (the First Additional Financing) under the Association's Fifth Dimension Program, which was established by the Association in its fiscal year 1989, consisting of supplemental credits financed by reflows to offset interest payments to the International Bank for Reconstruction and Development; and

WHEREAS (D) on the basis, *inter alia*, of the foregoing, the Association has decided in support of the Program to provide such assistance to the Borrower by making the credit provided for in Article II of this Agreement and the First Additional Financing (jointly, the Credit) 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 Development Credit Agreements" of the Association, dated January 1, 1985, (as amended through May 1, 2004) with the modifications set forth below (the General Conditions) constitute an integral part of this Agreement:

- (a) Section 2.01, paragraph 12, is modified to read:

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

- (b) Section 4.01 is modified to read:

“Except as the Borrower and the Association shall otherwise agree, withdrawals from the Credit Account shall be made in the currency of the deposit account specified in Section 2.02 of the Development Credit Agreement.”;

- (c) Section 5.01 is modified to read:

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

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

- (e) Section 9.06 (c) is modified to read:

“(c) Not later than six months after the Closing Date or such later date as may be agreed for this purpose between the Borrower and the Association, the Borrower shall prepare and furnish to the Association a report, of such scope and in such detail as the Association shall reasonably request, on the execution of the program referred to in the Preamble to the Development Credit Agreement, the performance by the Borrower and the Association of their respective obligations under the Development Credit Agreement and the accomplishment of the purposes of the Credit.”; and

- (f) Section 9.04 is deleted and Sections 9.05, 9.06 (as modified above), 9.07 and 9.08 are renumbered, respectively, Sections 9.04, 9.05, 9.06 and 9.07.

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) “CONAP” means *Consejo Nacional de Áreas Protegidas*, the Borrower’s national board for protected areas;
- (b) “Congress” means the legislative branch of government of the Borrower;
- (c) “Deposit Account” means the account referred to in Section 2.02 (b) of this Agreement;
- (d) “Executive” means the executive branch of government of the Borrower;
- (e) “Protected Area” means an area officially designated by the Borrower to be under a special management regime for the primary purpose of ensuring its biodiversity and ecological integrity;
- (f) “PRS” means the Borrower’s Poverty Reduction Strategy, as set forth in the PRSP;
- (g) “PRSP” means the Borrower’s Poverty Reduction Strategy Paper dated April, 2001, published in the website of the Borrower’s Ministry of the Presidency (*Secretaría de Estado del Despacho Presidencial*);
- (h) “SE” means *Secretaría de Estado en el Despacho de Educación*, the Borrower’s Ministry of Education;
- (i) “SEFIN” means *Secretaría de Estado en el Despacho de Finanzas*, the Borrower’s Ministry of Finance;
- (j) “SERNA” means *Secretaría de Estado en los Despachos de Recursos Naturales y Ambiente*, the Borrower’s Ministry of Natural Resources and Environment;
- (k) “SES” means *Secretaría de Estado en el Despacho de Salud*, the Borrower’s Ministry of Health;
- (l) “SGJ” means *Secretaría de Estado en los Despachos de Gobernación y Justicia*, the Borrower’s Ministry of Governance and Justice;
- (m) “SIAFI” means *Sistema Integrado de Administración Financiera*, the Borrower’s integrated financial management system;

(n) “SIARH” means *Sistema Integrado de Administración de Recursos Humanos*, the Borrower’s integrated human resources management system;

(o) “SIARHD” means *Sistema Integrado de Administración de Recursos Humanos Docentes*, the Borrower’s integrated teacher human resources management system; and

(p) “SINAPH” means *Sistema Nacional de Áreas Protegidas de Honduras*, the Borrower’s National Protected Areas System.

## ARTICLE II

### The Credit

Section 2.01. The Association agrees to lend to the Borrower, on the terms and conditions set forth or referred to in this Agreement, an amount in various currencies equivalent to forty million five hundred forty thousand Special Drawing Rights (SDR 40,540,000) (the Credit), which includes an original amount in various currencies equivalent to thirty eight million six hundred thousand Special Drawing Rights (SDR 38,600,000), and a first supplemental amount in various currencies equivalent to one million nine hundred forty thousand Special Drawing Rights (SDR 1,940,000) (the First Additional Financing).

Section 2.02. (a) Subject to the provisions of paragraphs (b) and (c) of this Section, the Borrower shall be entitled to withdraw the proceeds of the Credit from the Credit Account in support of the Program.

(b) The Borrower shall open, prior to furnishing to the Association the first request for withdrawal from the Credit Account, and thereafter maintain in its central bank, a deposit account in Dollars on terms and conditions satisfactory to the Association. All withdrawals from the Credit Account shall be deposited by the Association into the Deposit Account.

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

Section 2.03. The Closing Date shall be one year from the date of this Agreement or such later date as the Association shall establish. The Association shall promptly notify the Borrower of such later date, which later date shall in no case apply to the First Additional Financing.

Section 2.04. (a) The Borrower shall pay to the Association 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, 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 Borrower from the Credit Account or cancelled; 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 2.06 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 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 June 15 and December 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 June 15 and December 15 commencing December 15, 2014 and ending June 15, 2044. Each installment to and including the installment payable on June 15, 2024 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 the Association 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 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**

#### **Particular Covenants**

Section 3.01. (a) The Borrower and the Association shall from time to time, at the request of either party, exchange views on the progress achieved in carrying out the Program.

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

(c) Without limitation upon the provisions of paragraph (a) of this Section, the Borrower shall exchange views with the Association on any proposed action to be taken after the disbursement of the Credit 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 Association'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 Association;

(b) furnish to the Association as soon as available, but in any case not later than four months after the date of the Association'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 Association shall have reasonably requested; and

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



## **ARTICLE IV**

### **Additional Events of Suspension**

Section 4.01. Pursuant to Section 6.02 (l) of the General Conditions, the following additional events are specified:

(a) The Borrower's macroeconomic policy framework has become inconsistent with the objectives of the Program.

(b) An action has been taken or a policy has been adopted to materially reverse any action or policy under the Program in a manner that would, in the opinion of the Bank, adversely affect the achievements of the objectives of the Program.

(c) An action has been taken or a policy has been adopted to materially reverse any action listed in Schedule 2 to this Agreement.

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

## **ARTICLE V**

### **Termination**

Section 5.01. The date November 16, 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 Secretary of SEFIN is designated as the 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:

*Secretaría de Estado en el Despacho de Finanzas*  
Tegucigalpa, M.D.C.  
Honduras

	Cable address:	Facsimile:
4142	HACIENDA	(504) 237-
5033	Tegucigalpa	(504) 237-

For the Association:

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

	Cable address:	Telex:	Facsimile:
6391	INDEVAS	248423 (MCI) or	(202) 477-
	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 Tegucigalpa, Honduras, as of the day and year first above written.

REPUBLIC OF HONDURAS

By /s/ Arturo Alvarado

Authorized Representative

ASSOCIATION

INTERNATIONAL

DEVELOPMENT

By /s/ Joseph Owen

Authorized Representative

Honorary Witness on behalf of  
the Republic of Honduras:

/s/ Ricardo Maduro  
President of the Republic of Honduras

## SCHEDULE 1

### Excluded Expenditures

For purposes of Section 2.02 (c) of this Agreement, the proceeds of the Credit 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 Association or the Bank shall have financed or agreed to finance under another credit or a loan;
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 Association 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 manufactured	-	Tobacco,  (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 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 Association determines that corrupt or fraudulent practices were engaged in by representatives of the Borrower or of a beneficiary of the Credit during the procurement or execution of such contract, without

the Borrower having taken timely and appropriate action satisfactory to the Association to remedy the situation.

## SCHEDULE 2

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

#### I. Pro-Poor Growth – Increasing Investment and Employment

##### A. Investment Climate and Competitiveness

1. The Borrower has satisfactorily implemented the Administration Simplification Law (*Ley de Simplificación Administrativa*; Decree No. 255-2002 published in the Borrower's Official Gazette on August 10, 2002), as evidenced by the following:

(a) the time to register a typical business in Tegucigalpa has been reduced from 129 days in the year 2002 to 62 days in the first quarter of the year 2004; and

(b) the creation of a national administrative simplification committee (*Comité Nacional de Simplificación Administrativa*), through an executive decree (*Decreto Ejecutivo*) and a resolution adopted by the Borrower's National Competitiveness Commission, to coordinate all initiatives for administrative simplification.

2. (a) Following consultations with the private sector and other stakeholders and negotiations with the concessionaire, the Congress has issued a decree approving an amendment to the airport concession contract for the Honduran airports, thereby improving the efficiency, quality and regional competitiveness of Honduran airports; and

(b) the Executive has issued a decree appointing a public-private monitoring committee to follow up on implementation of the amended airport concession contract referred to in the preceding paragraph.

3. The Borrower has increased access and efficiency in telecommunications services through the following actions:

(a) *HONDUTEL* (the Borrower's telecommunications company) has awarded 27 commercialization contracts and 4 interconnection contracts for private operators to provide market-priced, national and local call services; and

(b) *CONATEL* (the Borrower's National Commission for Telecommunications) has awarded a license to a second cellular telephone operator.

##### B. Land Rights and Access

The Congress has approved a property law, which establishes a unified property registry and strengthens and consolidates the laws and institutional arrangements for land regularization.

## II. Human Capital and Social Protection

### A. Education

1. Local education development associations (*Asociaciones de Desarrollo Educativo Local* or *ADELs*), which are non-profit associations comprised of the school principal and representatives of teachers, parents and students of a public school, empowered to administer, on behalf of SE, the provision of pre-school education and/or lower basic education in such public schools, have been legally established (with legal standing (*personería jurídica*) or with a statement from SGJ certifying that the procedure to grant legal standing is in process) in at least 2,700 rural schools.

2. The Borrower has published in SE's website and has submitted to its National Institute of Statistics (*Instituto Nacional de Estadística*):

(a) the educational statistics database from the 2003 school census, including the analysis of teacher and student distributions; and

(b) the teacher's payroll by department as it appears in SIARHD.

### B. Health

1. The SES has internally audited at least 30 percent of its human resource staff registries and has adjusted such registries to show the functional assignment of each staff member (where the person really works).

2. The SES has made budgetary allocations to pay the salaries of the 30 percent of its human resource staff appearing in the registries that have been internally audited, in a manner consistent with the registry.

3. The SES has issued a resolution stating that personnel transfers will not be permitted without the authorization of departmental directors and, if applicable, hospital directors.



### III. Sustainability – Public Sector Management, Governance and Environmental Sustainability

#### A. Public Resource Management

1. The Executive has redefined poverty reduction expenditures in the PRSP first annual progress report to improve linkage between poverty spending and PRS targets.
2. The Congress has passed a SIAFI law that mandates the use of SIAFI in all central government agencies and includes provisions for multi-annual budgeting, public sector accounting standards and internal controls.

#### B. Civil Service Reform

1. The Congress has passed a law (*Ley de Reordenamiento del Sistema Retributivo del Gobierno Central*) restoring the Executive's control over civil service wage management.
2. The Executive has presented to Congress legislation which:
  - (a) provides the basis for a professional civil service, including merit-based recruitment and promotion;
  - (b) places limits on the number of political appointments in the civil service; and
  - (c) creates a supervisory authority to regulate human resource management of the Borrower's central government.

#### C. Environmental Sustainability

1. SERNA has submitted to CONAP a strategic framework and action plan for the SINAPH Protected Areas, as well as a long-term financing strategy.
2. The Executive has prepared a draft agreement for the creation of a Protected Areas trust fund (*fideicomiso*) to finance the protection and

management expenditures in priority SINAPH Protected Areas by government and non-government sources.

IV. Monitoring and Evaluation of the Poverty Reduction Strategy

A. The Executive has completed and submitted to the Association the first annual PRSP progress report.

B. The Congress has amended the Poverty Reduction Support Law (*Ley del Fondo para la Reducción de la Pobreza*; Congressional Decree No. 70-2002 dated April 2, 2002).

C. The Executive has established within SIAFI a satisfactory mechanism to track the use of funds received under the “Heavily Indebted Poor Countries” or “HIPC” initiative launched by the Association and the International Monetary Fund in 1996.