

**CONFORMED COPY
LOAN NUMBER 7201-CO**

Loan Agreement

(Second Programmatic Fiscal and Institutional Structural Adjustment Loan)

between

REPUBLIC OF COLOMBIA

and

**INTERNATIONAL BANK FOR RECONSTRUCTION
AND DEVELOPMENT**

Dated November 24, 2003

LOAN NUMBER 7201-CO

LOAN AGREEMENT

AGREEMENT, dated November 24, 2003, between the REPUBLIC OF COLOMBIA (the Borrower) and INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT (the Bank).

WHEREAS (A) the Bank has received a letter, dated October 20, 2003, from the Borrower: (i) describing its macroeconomic framework and a program of actions, objectives and policies for fiscal and institutional reform, covering fiscal sustainability, public expenditure management, institutional reform and management of public liabilities (the Program), which Program consists of actions that have already been taken as described in Schedule 3 to this Agreement (the Second Phase of the Program), and actions and policies that the Borrower intends to take and adopt in the near future; (ii) declaring the Borrower's commitment to the objectives of the Program; and (iii) requesting assistance from the Bank in support of the Program during the execution thereof; and

WHEREAS (B) on the basis, *inter alia*, of the foregoing, the Bank has decided in support of the Second Phase of the Program to provide such assistance to the Borrower by making the loan provided for in Article II of this Agreement (the Loan) 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 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 Second Phase of 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 of the Loan from the Loan Account shall be made in the Loan Currency of such amount. If the Loan Currency is not the currency of the deposit account specified in Section 2.02 of the Loan Agreement, the Bank, at the request and acting as an agent of the Borrower, shall purchase with the Loan Currency withdrawn from the Loan Account the currency of such deposit account as shall be required to deposit the withdrawn amount into such deposit account.”

- (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) 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 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 Second Phase 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) “Asset Management” means the Borrower’s institutional and legal framework to account for, manage, allocate, maintain, use and dispose of government assets;

(b) “Central Bank” means *Banco de la República*, the Borrower’s central bank;

(c) “CONPES” means *Consejo Nacional de Política Económica y Social*, the Borrower’s National Council for Economic and Social Policy;

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

(e) “DIAN” means *Dirección de Impuestos y Aduanas Nacionales*, the Borrower’s Directorate of National Taxes and Customs;

(f) “DNP” means *Departamento Nacional de Planeación*, the Borrower’s Planning Department;

(g) “ICBF” means *Instituto Colombiano de Bienestar Familiar*, the Borrower’s Family Welfare Institute;

(h) “Law 21” means *Ley de Régimen del Subsidio Familiar*, the Borrower’s Family Subsidy Law, dated January 22, 1982, and duly published in the Borrower’s Official Gazette on February 5, 1982;

(i) “Law 80” means *Estatuto General de Contratación de la Administración Pública*, the Borrower’s Public Procurement Law, dated October 28, 1993, and duly published in the Borrower’s Official Gazette on October 28, 1993;

(j) “Law 788” means *Ley de Reforma Tributaria*, the Borrower’s Tax Reform Law, dated December 27, 2002, and duly published in the Borrower’s Official Gazette on December 27, 2002;

(k) “Law 819” means *Ley de Responsabilidad Fiscal*, the Borrower’s Fiscal Responsibility Law, dated July 9, 2003, and duly published in the Borrower’s Official Gazette on July 9, 2003;

(l) “MHCP” means *Ministerio de Hacienda y Crédito Público*, the Borrower’s Ministry of Finance and Public Credit;

(m) “Referendum” means the Borrower’s popular consultation process, by which the Borrower’s population votes to approve or reject, *inter alia*: (a) laws; (b) authorities’ decisions; (c) constitutional reforms; and (d) constitutional assemblies; and

(n) "SENA" means *Servicio Nacional de Aprendizaje*, the Borrower's Learning National Service.

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 this Agreement, an amount equal to one hundred fifty million Dollars (\$150,000,000), 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) and (c) of this Section, the Borrower shall be entitled to withdraw the amount of one hundred forty-eight million five hundred thousand Dollars (\$148,500,000) from the Loan Account in support of the Second Phase 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 the Central Bank, a deposit account in Dollars on terms and conditions satisfactory to the Bank. All withdrawals of the amount referred to in paragraph (a) above shall be deposited by the Bank into the Deposit Account.

(c) 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 February 25, 2004, 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 front-end fee in an amount equal to one percent (1%) of the amount of the Loan. On or promptly after the Effective Date, the Bank shall, on behalf of the Borrower, withdraw from the Loan Account and pay to itself the amount of said fee.

Section 2.05. The Borrower shall pay to the Bank a commitment charge on the principal amount of the Loan not withdrawn from time to time, at a rate equal to: (a) eighty five one-hundredths of one per cent (0.85%) per annum from the date on which such charge commences to accrue in accordance with the provisions of Section 3.02 of the General Conditions to, but not including, the fourth anniversary of such date; and (b) seventy five one-hundredths of one per cent (0.75%) per annum thereafter.

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 commitment charges shall be payable semiannually in arrears on May 15 and November 15 in each year.

Section 2.08. The Borrower shall repay the principal amount of the Loan in accordance with the provisions of Schedule 2 to this Agreement.

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.

Section 2.10. Without limitation upon the provisions of paragraph (a) of Section 2.09 of this Agreement and unless otherwise notified by the Borrower to the Bank in accordance with the provisions of the Conversion Guidelines, the interest rate basis applicable to the aggregate principal amount of the Loan withdrawn during each Interest Period shall be changed from the initial Variable Rate to a Fixed Rate for the full maturity of such amount 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 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.

(b) 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.

(c) Without limitation upon the provisions of paragraph (a) 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 3 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 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 Events of Suspension

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

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

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

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

(d) An action has been taken or a policy has been adopted to reverse any action listed in Schedule 3 to this Agreement.

ARTICLE V

Termination

Section 5.01. The date February 24, 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 and Public Credit 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 and Public Credit
Carrera 7-A. No. 6-45, Piso 8
Bogotá, República de Colombia

Facsimile:

57-1-350-9344
57-1-297-1578

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

REPUBLIC OF COLOMBIA

By/s/ Alberto Moreno

Authorized Representative

INTERNATIONAL BANK FOR
RECONSTRUCTION AND DEVELOPMENT

By/s/ David de Ferranti

Regional Vice President
Latin America and the Caribbean

SCHEDULE 1

Excluded Expenditures

For purposes of Section 2.02 (c) 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

Amortization Schedule

1. The following table sets forth the Principal Payment Dates of the Loan and the percentage of the total principal amount of the Loan payable on each Principal Payment Date (Installment Share). If the proceeds of the Loan shall have been fully withdrawn as of the first Principal Payment Date, the principal amount of the Loan repayable by the Borrower on each Principal Payment Date shall be determined by the Bank by multiplying: (a) the total principal amount of the Loan withdrawn and outstanding as of the first Principal Payment Date; by (b) the Installment Share for each Principal Payment Date, such repayment amount to be adjusted, as necessary, to deduct any amounts referred to in paragraph 4 of this Schedule, to which a Currency Conversion applies.

| <u>Payment Date</u> | <u>Installment Share (Expressed as a %)</u> |
|---------------------|---|
| 15-Nov-2009 | 10% |
| 15-Nov-2010 | 10% |
| 15-Nov-2011 | 10% |
| 15-Nov-2012 | 10% |
| 15-Nov-2013 | 10% |
| 15-Nov-2015 | 10% |
| 15-Nov-2016 | 10% |
| 15-Nov-2017 | 10% |
| 15-Nov-2018 | 10% |
| 15-Nov-2019 | 10% |

2. If the proceeds of the Loan shall not have been fully withdrawn as of the first Principal Payment Date, the principal amount of the Loan repayable by the Borrower on each Principal Payment Date shall be determined as follows:

(a) To the extent that any proceeds of the Loan shall have been withdrawn as of the first Principal Payment Date, the Borrower shall repay the amount withdrawn and outstanding as of such date in accordance with paragraph 1 of this Schedule.

(b) Any withdrawal made after the first Principal Payment Date shall be repaid on each Principal Payment Date falling after the date of such withdrawal in amounts determined by the Bank by multiplying the amount of each such withdrawal by a fraction, the numerator of which shall be the original Installment Share specified in the

table in paragraph 1 of this Schedule for said Principal Payment Date (the Original Installment Share) and the denominator of which shall be the sum of all remaining Original Installment Shares for Principal Payment Dates falling on or after such date, such repayment amounts to be adjusted, as necessary, to deduct any amounts referred to in paragraph 4 of this Schedule, to which a Currency Conversion applies.

3. (a) Withdrawals made within two (2) calendar months prior to any Principal Payment Date shall, for the purposes solely of calculating the principal amounts payable on any Principal Payment Date, be treated as withdrawn and outstanding on the second Principal Payment Date following the date of withdrawal and shall be repayable on each Principal Payment Date commencing with the second Principal Payment Date following the date of withdrawal.

(b) Notwithstanding the provisions of subparagraph (a) of this paragraph 3, if at any time the Bank shall adopt a due date billing system under which invoices are issued on or after the respective Principal Payment Date, the provisions of such subparagraph shall no longer apply to any withdrawals made after the adoption of such billing system.

4. Notwithstanding the provisions of paragraphs 1 and 2 of this Schedule, upon a Currency Conversion of all or any portion of the withdrawn principal amount of the Loan 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 determines in accordance with the Conversion Guidelines, the exchange rate component of the Screen Rate.

5. If the principal amount of the Loan withdrawn and outstanding from time to time shall be denominated in more than one Loan Currency, the provisions of this Schedule shall apply separately to the amount denominated in each Loan Currency, so as to produce a separate amortization schedule for each such amount.

SCHEDULE 3

Second Phase of the Program

1. The execution of the Borrower's national central government budget for the year 2003, through the end of the third calendar quarter, prior to Loan initial disbursements, has not exceeded 75% of the overall deficit limit in said budget.
2. The Borrower has issued the necessary executive decrees to regulate the application of Law 788.
3. The Borrower, through DIAN, has: (a) developed and implemented software to cross reference information with financial institutions to ensure that interest reported by them match interest reported by taxpayers; (b) audited at least 50% of large taxpayers (as defined in Article 562 of the Borrower's tax code) affected by the new taxes; (c) established and published indicators of the cost and time required for tax filing compliance by taxpayers; and (d) has carried out at least 80 integrated tax and customs audits.
4. The Borrower has approved CONPES document number 3252 dated October 20, 2003, that outlines the strategy for national central government budget reform, including, *inter alia*: (a) the elimination or reduction of permanent entitlements and earmarked revenues; (b) the regulation of the use of forward budgeting; and (c) the establishment of controls over expenditure aggregates.
5. The Borrower's Executive Branch has submitted to the Borrower's Congress and said Congress has approved, the 2004 budget bill of law, to approve the Borrower's 2004 public budget, to include, *inter alia*: (a) medium term fiscal outlooks; (b) the calculation of tax expenditures and contingent liabilities; and (c) the presentation by functions of the Borrower's government sector, integrating current and capital Borrower's government expenditures.
6. The Borrower has submitted to popular vote the provision of the Referendum that reallocates royalty transfers to educational services.
7. The Borrower's Ministry of Education has issued a resolution (Resolution Number 277/03, dated February 17, 2003), to establish the eligibility criteria to allocate economic resources generated from the application of Law 21 for the benefit of public education infrastructure projects in the Borrower's territory.

8. The Borrower has approved CONPES document number 3250, dated October 20, 2003, establishing, *inter alia*, the new policy for legal defense of the state, including legal reform if necessary.
9. The Borrower has approved CONPES document number 3249, dated October 20, 2003, establishing, *inter alia*: (a) the principles that apply to government public procurement; (b) the creation of a new agency or the assignment to an existing agency of public sector procurement responsibilities; and (c) the definition of a strategy for developing and implementing e-procurement.
10. The Borrower has proposed to its legislature modifications to the bill of law amending Law 80 that incorporate the recommendations of CONPES, including, *inter alia*: (a) common principles for public procurement; (b) introduction of economic considerations into the public procurement process; and (c) institutional framework for public procurement.
11. The Borrower has approved CONPES document number 3251, dated October 20, 2003, establishing the basic principles and strategic planning for Asset Management, including, *inter alia*: (a) the institutional framework for Asset Management; (b) the management information systems required for Asset Management; and (c) the rules and procedures for Asset Management.
12. The Borrower, through MHCP and DNP, has signed pilot management agreements with SENA and ICBF.
13. The Borrower has approved CONPES document number 3248 dated October 20, 2003, establishing the overall strategy of public sector reform and a recommendation to design indicators on public sector productivity and effectiveness.
14. The Borrower has developed a monitoring and evaluation system for the state reform process with indicators of productivity and effectiveness and has widely publicized it, including its publication through DNP's web site.
15. The Borrower has enacted Law Number 819 that regulates, *inter alia*: (a) the annual presentation of: (i) a medium-term fiscal framework with deficit targets linked to debt sustainability; (ii) a report of fiscal results to congress (including all debt and contingent liabilities); and (iii) a financial plan that includes measures to fully compensate for any fiscal slippage in the previous year; (b) restrictions on future spending obligations of national and sub-national governments; and (c) the obligation to include the fiscal impact and source of financing within any new national law that affects taxes or expenditures.

