

CONFORMED COPY

LOAN NUMBER 7210-PA

Loan Agreement

(Economic Recovery Structural Adjustment Loan)

between the

REPUBLIC OF PARAGUAY

and

**INTERNATIONAL BANK FOR RECONSTRUCTION
AND DEVELOPMENT**

Dated December 16, 2003

LOAN NUMBER 7210-PA

LOAN AGREEMENT

AGREEMENT, dated December 16, 2003, between the REPUBLIC OF PARAGUAY (the Borrower) and INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT (the Bank).

WHEREAS (A) the Bank has received from the Borrower a letter, dated November 19, 2003, describing a program of actions, objectives and policies designed to achieve structural adjustment of the Borrower's economy (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;

(B) the Borrower has carried out the measures and taken the actions described in Schedule 3 to this Agreement to the satisfaction of the Bank and has maintained a macroeconomic policy framework satisfactory to the Bank; and

(C) 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 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 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Loan Agreement, the Bank, at the request and acting as an agent of the Borrower, shall purchase with the Loan Currency withdrawn from the Loan Account the currency of such deposit account as shall be required to deposit the withdrawn amount into such deposit account.”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 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) “Central Administration” means the Borrower’s Executive, Judicial and Legislative Powers, the Comptroller General, the Office of the Public Defender, and the Treasury;

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

(c) “Guaraníes” means the currency of the Borrower; and

(d) “*Unidad Central Normativa y Técnica*” means the unit established by Law 205/2003 regulated by Decree No. 21909/2003 where said unit is defined as *Dirección General de Contrataciones Públicas* (DGCP).

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 thirty million Dollars (\$30,000,000), 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 twenty nine million seven hundred thousand Dollars (\$29,700,000) from the Loan Account 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. All withdrawals from the Loan Account 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 December 31, 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 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: (i) 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 (ii) 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 April 15 and October 15 in each year.

Section 2.08. The Borrower shall repay the principal amount of the Loan in accordance with the provisions of Schedule 3 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.
- (c) Promptly following the Execution Date for an Interest Rate Caps or Interest Rate Collar in respect of which the Borrower has requested that the premium be paid out of the proceeds of the Loan, the Bank shall, on behalf of the Borrower, withdraw from the Loan Account and pay to itself the amounts required to pay any premium payable in accordance with Section 4.04(c) of the General Conditions up to the amount

allocated from time to time for such purpose in the table in paragraph 1 of Schedule 1 to this Agreement.

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 Event of Suspension

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

(a) Namely, that 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 achievements 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 March 15, 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:

Minister of Finance
(*Ministerio de Hacienda*)
Chile 128 casi Palma
Asunción, Paraguay

Facsimile: 595 (21) 448-283

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 PARAGUAY

By /s/ Dionisio Borda

Minister of Finance

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>
On each April 15 and October 15	
Beginning April 15 2009 through April 15 2026	2.78 %
On October 15, 2026	2.70 %

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 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 sub-paragraph (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 sub-paragraph 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

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

1. The Borrower's executive branch has withdrawn supplemental budget requests presented to the Borrower's Congress during calendar year 2003 for an amount of *Guaraníes* 197,223,910,919 with the exception of requests for the purpose of external debt payments and social sectors expenditures.
2. The Borrower has not increased Central Administration salaries as evidenced by budget execution reports corresponding to the period August to October 2003.
3. The Borrower has ensured that 60% (totaling 125,000) of all public employees in Central Administration agencies have been checked for duplicative salary payments. 1,650 have been identified as holding more than one job, and the Borrower has set up a system to regularize their situation via elimination of extra positions.
4. The Borrower has increased the excise tax on diesel oil to 20% by issuance of Decree No. 21799, dated July 28, 2003.
5. A draft-law for the Borrower's national annual budget for calendar year 2004 (*Presupuesto General de la Nación – Ejercicio Fiscal 2004*) has been submitted to Congress, and such budget is consistent with the attainment of a primary surplus in the Central Administration and shifts to program and results format.
6. The Borrower has adopted measures to combat tax evasion, including: (i) the removal of all non-customs employees from customs areas; (ii) the elimination of ad-hoc checkpoints along transport routes; (iii) the creation of a special technical unit combining staff from the Public Prosecutor's Office (*Ministerio Público*), and the ministries of the Interior, Finance and Industry and Commerce in order to improve coordination of efforts on combating tax evasion and informality of the Borrower's economy; and (iv) the launching of an educational and awareness-raising campaign for tax compliance, all by means of the following Borrower's decrees: (i) Decree No. 87, dated August 19, 2003; (ii) Decree No. 88, dated August 19, 2003; (iii) Decree No. 527, dated October 9, 2003; and (iv) Inter-ministerial Cooperation Agreement entered into between the Minister of Finance and the Minister of Education and Culture on September 25, 2003.
7. A draft law for a new Customs Code has been submitted to Congress, including measures for renewal and simplification of administrative procedures, promotion of selective audits, the granting of financial autonomy to the Customs Administration and the professionalization of its staff.
8. A draft law on administrative and tax reform (*Reordenamiento Administrativo y Adecuación Fiscal*) has been submitted to Congress, including the following measures: (i) widening of the value added tax (VAT) base through generalization of VAT to

agriculture, services, and current contributors to the *Unified Tax (Tributo Unico)*; (ii) reduction of exemptions; (iii) increase in the excise tax on alcohol and cigarettes; (iv) reduction of the income tax rate on firms and a widening of the income tax base.

9. Regarding public sector procurement, the Borrower has: (i) issued Decree No. 21909, dated August 11, 2003 for the regulation of Law No. 2051/2003; (ii) issued Ministerial Resolution No. 138, dated October 15, 2003 which creates the Directorate General of Public Procurement (DGCP) in the Ministry of Finance; and (iii) ensured that the contents of Decree No. 21909 mentioned under 9 (i) above, has been disseminated.

10. The Borrower has adopted a Procurement Action Plan that includes development and implementation of: (i) the institutional and operational framework for the DGCP and the agency procurement units; (ii) a human resources development plan; (iii) an electronic information and procurement system; and (iv) strengthened contract management.

11. The Borrower has signed an agreement with Transparency Paraguay for actions to improve the transparency of public resource use in the Ministry of Finance on September 5, 2003.

12. A Census of employees in the public sector has been launched by means of Decree No. 265, dated September 11, 2003 in order to determine the number of public employees and their positions.

13. The Borrower has created the Central Unit of Public Investment in the Ministry of Finance (*Unidad Central de Inversión Pública*) by means of Ministerial Resolution No. 78, dated September 25, 2003.

14. The Borrower has adopted a financial management action plan, including the following measures : (i) introduction of accrual accounting in the Integrated System of Financial Management (*Sistema Integrado de Administración Financiera (SIAF)*) system; and (ii) implementation of SIAF in the public decentralized agencies of the non-financial sector.

15. The Borrower's Deposit Guarantee and Bank Resolution Fund (*Fondo de Garantía de Depósitos y Resoluciones Bancarias*) is in effect.

16. Public bidding has been launched to hire technical assistance to: (i) design a database for the Borrower's Public Sector Pension System (*Caja Fiscal*) and to digitalize contributor and beneficiary files; and (ii) design a process for the restructuring of contributory and non-contributory pensions of said System.

17. A draft law for reforming the Public Sector Pension System has been submitted to Congress, including the following measures: (i) increase of the retirement age; (ii) lengthening of the time period over which the salary base for pension benefits is

calculated; (iii) reduction in replacement rates for mandatory and early retirement; (iv) raising of the age and years of contribution required for early retirement; and (v) harmonization of contributions and benefits of the Public Sector Pension System with those of other existing pension funds.