

CONFORMED COPY

CREDIT NUMBER 3533 BOS

Development Credit Agreement

(Second Local Initiatives (Microfinance) Project)

between

BOSNIA AND HERZEGOVINA

and

INTERNATIONAL DEVELOPMENT ASSOCIATION

Dated October 19, 2001

CREDIT NUMBER 3533 BOS

DEVELOPMENT CREDIT AGREEMENT

AGREEMENT, dated October 19, 2001, between BOSNIA AND HERZEGOVINA (the Borrower) and INTERNATIONAL DEVELOPMENT ASSOCIATION (the Association).

WHEREAS (A) the Borrower, having satisfied itself as to the feasibility and priority of the Project described in Schedule 2 to this Agreement, has requested the Association to assist in the financing of the Project;

(B) Part A of the Project will be carried out by the Federation of Bosnia and Herzegovina (the Federation) with the Borrower's assistance and, as part of such assistance, the Borrower will make available to the Federation a part of the proceeds of the Credit as provided in this Agreement;

(C) Part B of the Project will be carried out by Republika Srpska (RS) with the Borrower's assistance and, as part of such assistance, the Borrower will make available to RS a part of the proceeds of the Credit as provided in this Agreement;

WHEREAS the Association has agreed, on the basis, inter alia, of the foregoing, to extend the Credit to the Borrower upon the terms and conditions set forth in this Agreement and in the Project Agreements of even date herewith between the Association and the Federation and the Association and Republika Srpska;

NOW THEREFORE the parties hereto hereby agree as follows:

ARTICLE I

## General Conditions; Definitions

Section 1.01. The "General Conditions Applicable to Development Credit Agreements" of the Association, dated January 1, 1985 (as amended through October 6, 1999), with the modifications set forth below (the General Conditions), constitute an integral part of this Agreement.

(a) A new paragraph (12) is added to Section 2.01 to read as set forth below, and the existing paragraphs (12) through (14) of said Section are accordingly renumbered as paragraphs (13) through (15):

"12. 'Participating Country' means any country that the Association determines meets the requirements set forth in Section 11 of Resolution No. 194 of the Board of Governors of the Association, adopted on April 8, 1999; and 'Participating Countries' means, collectively, all such countries."; and

(b) The second sentence of Section 5.01 is modified to read:

"Except as the Borrower and the Association shall otherwise agree, no withdrawals shall be made: (a) on account of expenditures in the territories of any country which is not a Participating Country or for goods produced in, or services supplied from, such territories; or (b) for the purpose of any payment to persons or entities, or for any import of goods, if such payment or import, to the knowledge of the Association, is prohibited by a decision of the United Nations Security Council taken under Chapter VII of the Charter of the United Nations."

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) "DEF" means the Development and Employment Foundation of the Republika Srpska created through Government Decree No. 02/1-020-861/00, dated September 5, 2000, selected to act as an executing agency on behalf of the Republika Srpska for the purposes of on-lending the respective portion of the proceeds of the Credit to MCOs as provided in Schedule 1 of the Republika Srpska Project Agreement;

(b) "Eligible Categories" means, in respect of the Federation Special Account for Part A of the Project, Categories A (1) and A (2) set forth in the table in Part A.1 of Schedule 1 to this Agreement; and in respect of the Republika Srpska Special Account for Part B of the Project, Categories B (1) and B (2) set forth in the table in Part A.1 of Schedule 1 to this Agreement;

(c) "Eligible Expenditures" means, in respect of the Federation Special Account for Part A of the Project, the amounts paid by an MCO on account of withdrawals made by a Sub-borrower under a Microcredit to meet the reasonable cost of goods and services required for a Qualifying Project Activity under Part A.1 of the Project and to be financed out of the proceeds of the Credit allocated from time to time to said Special Account's respective Eligible Categories; and in respect of the Republika Srpska Special Account for Part B of the Project, the amounts paid by an MCO on account of withdrawals made by a Sub-borrower under a Microcredit to meet the reasonable cost of goods and services required for a Qualifying Project Activity under Part B.1 of the Project and to be financed out of the proceeds of the Credit allocated from time to time to said Special Account's respective Eligible Categories;

(d) "Entity" means either the Federation (defined hereinafter) or Republika Srpska, as the case may be, and "Entities" means the Federation and Republika Srpska, collectively;

(e) "Euro" means the lawful currency of the member states of the European Union that adopt the single currency in accordance with the Treaty establishing the European Community, as amended by the Treaty on European Union;

(f) "Federation" means the Federation of Bosnia and Herzegovina, a political subdivision of the Borrower, and includes any successor or successors thereto;

(g) "Federation Project Agreement" means the agreement between the Association and the Federation of even date herewith, as the same may be amended from time to time, and such term includes all schedules and agreements supplemental to the Federation Project Agreement;

(h) "FSD" means the foundation for sustainable development to be established in the Federation BH through a merger between the Federation Employment and Training Foundation created through Government Decree (Official Gazette of the Federation BH No. 14/1996, dated August 16, 1996, 2000), and the Federation Local Development Foundation created through Government Decree (Official Gazette of the Federation BH No. 23/1999, dated June 21, 1999), and selected to act as an executing agency on behalf of the Federation BH for the purposes of on-lending the respective portion of the proceeds of the Credit to MCOs as provided in Schedule 1 of the Federation Project Agreement;

(i) "MCO" or "Microcredit Organization" means an organization authorized to engage in microfinance activities in accordance with the Microcredit Organization Law;

(j) "Microcredit" means a credit made or proposed to be made to a Sub-borrower out of the proceeds of the Credit by an MCO, under a Microcredit Agreement (as hereinafter defined), pursuant to the provisions of the Attachment to the Annex to Schedule 1 to the Project Agreements, to finance a Qualifying Project Activity; and the term "Microcredits" means, collectively, more than one Microcredit;

(k) "Microcredit Agreement" means an agreement to be entered into between an MCO and a Sub-borrower in respect of a Qualifying Project Activity to be financed out of the proceeds of a Microcredit;

(l) "Microcredit Organization Law" means, in the case of the Federation, the Law on Microcredit Organizations published in the Official Gazette of the Federation BH No. 24/00, and in the case of the Republika Srpska, the Law on Microcredit Organizations published in the Official Gazette of the RS No. 19 dated May 11, 2001;

(m) "Operational Guidelines" means the guidelines adopted by the Federation FSD and RS DEF and referred to in paragraph 1 of Schedule 1 to the Project Agreements, setting out the operational and administrative procedures for the implementation of the Project including selection, financing, monitoring and performance assessment of MCOs and criteria for the selection of Qualifying Project Activities;

(n) "Project Agreement" means either the Federation Project Agreement or the Republika Srpska Project Agreement, as the case may be, and "Project Agreements" means said project agreements, collectively;

(o) "Project Management Report" means each report prepared in accordance with Section 3.02 of the Federation Project Agreement and Republika Srpska Project Agreement;

(p) "Qualifying Project Activity" means a specific activity selected for financing under Parts A.1 and B.1 of the Project in accordance with the Operational Guidelines and the provisions of the Project Agreements;

(q) "Republika Srpska" or "RS" means Republika Srpska, a political subdivision of the Borrower, and includes any successor or successors thereto;

(r) "RS Project Agreement" means the agreement between the Association and Republika Srpska of even date herewith, as the same may be amended from time to time, and such term includes all schedules and agreements supplemental to the RS Project Agreement;

(s) "Special Accounts" means the accounts referred to in Part B of Schedule 1 to this Agreement;

(t) "Sub-borrower" means a natural person or legal entity to which a Microcredit Organization is permitted to lend Microcredits under the Microcredit Organization Law in their respective entity and in accordance with any regulations adopted pursuant thereto;

(u) "Subsidiary Financing and Project Implementation Agreement" means either agreement to be entered into between the Borrower and each Entity pursuant to Section 3.01 (b) or (c) of this Agreement, as the same may be amended from time to time, and such term includes all schedules to each Subsidiary Financing and Project Implementation Agreement; "Subsidiary Financing and Project Implementation Agreements" means said agreements, collectively; and "Subsidiary Credit" means a credit to be made out of the proceeds of the Credit provided to each Entity under a Subsidiary Financing and Project Implementation Agreement; and "Sub-credit" means a credit to be made available out of the proceeds of the Subsidiary Credit provided to the Federation FSD and RS DEF under a Subsidiary Financing and Project Implementation Agreement;

(v) "Subsidiary Loan" means any loan made pursuant to a Subsidiary Loan Agreement (as hereinafter defined); and

(w) "Subsidiary Loan Agreement" means any agreement entered or to be entered into between the Federation FSD or RS DEF and an MCO pursuant to paragraph B.2 of the Annex to Schedule 1 to the Federation and RS Project Agreements, as the same may be amended from time to time, and such term includes all schedules supplemental to the Subsidiary Loan Agreement.

## 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 the Development Credit Agreement, an amount in various currencies equivalent to fifteen million eight hundred thousand Special Drawing Rights (SDR 15,800,000).

Section 2.02. (a) The amount of the Credit may be withdrawn from the Credit Account in accordance with the provisions of Schedule 1 to this Agreement for: (i) expenditures made (or, if the Association shall so agree, to be made) in respect of the reasonable cost of the services required for the Project and to be financed out of the proceeds of the Credit; and (ii) amounts paid (or, if the Association shall so agree, amounts to be paid) by an MCO on account of withdrawals made by a Sub-borrower under a Microcredit to meet the reasonable cost of goods and services required for a Qualifying Project Activity under Parts A.1 and B.1 of the Project in respect of which withdrawal from the Credit Account is requested.

Section 2.03. The Closing Date shall be June 30, 2005, or such later date as the Association shall establish. The Association shall promptly notify the Borrower of such later date.

Section 2.04. (a) The Borrower shall pay to the Association 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 canceled; 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 April 15 and October 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 April 15 and October 15, commencing October 15, 2011, and ending April 15, 2036. Each installment to and including the installment payable on April 15, 2021, shall be one and one-fourth percent (1-1/4%) of such principal amount, and each installment thereafter shall be two and one-half percent (2-1/2%) of such principal amount.

(b) Whenever: (i) the Borrower's per capita gross national product (GNP), as determined by the Association, shall have exceeded for three consecutive years the level established annually by the Association for determining eligibility to access the Association's resources; and (ii) the Bank shall consider the Borrower creditworthy for Bank lending, the Association may, subsequent to the review and

approval thereof by the Executive Directors of the Association and after due consideration by them of the development of the Borrower's economy, modify the repayment of installments under paragraph (a) above by: (A) requiring the Borrower to repay twice the amount of each such installment not yet due until the principal amount of the Credit shall have been repaid; and (B) requiring the Borrower to commence repayment of the principal amount of the Credit as of the first semiannual payment date referred to in paragraph (a) above falling six months or more after the date on which the Association notifies the Borrower that the events set out in this paragraph (b) have occurred, provided, however, that there shall be a grace period of a minimum of five years on such repayment of principal.

(c) If so requested by the Borrower, the Association may revise the modification referred to in paragraph (b) above to include, in lieu of some or all of the increase in the amounts of such installments, the payment of interest at an annual rate agreed with the Association on the principal amount of the Credit withdrawn and outstanding from time to time, provided that, in the judgment of the Association, such revision shall not change the grant element obtained under the above-mentioned repayment modification.

(d) If, at any time after a modification of terms pursuant to paragraph (b) above, the Association determines that the Borrower's economic condition has deteriorated significantly, the Association may, if so requested by the Borrower, further modify the terms of repayment to conform to the schedule of installments as provided in paragraph (a) above.

Section 2.08. Euro is hereby specified for the purposes of Section 4.02 of the General Conditions.

### ARTICLE III

#### Execution of the Project

Section 3.01. (a) The Borrower declares its commitment to the objectives of the Project as set forth in Schedule 2 to this Agreement, and, to this end, without any limitation or restriction upon any of its other obligations under the Development Credit Agreement, shall cause the Federation and Republika Srpska to perform in accordance with the provisions of the Federation Project Agreement and the RS Project Agreement, respectively, all of the obligations of the Federation and Republika Srpska therein set forth, shall take and cause to be taken all actions, including the provision of funds, facilities, services and other resources necessary or appropriate to enable the Federation and Republika Srpska to perform such obligations, and shall not take or permit to be taken any action which would prevent or interfere with such performance.

(b) For the purposes of Part A of the Project, the Borrower shall enter into a subsidiary financing and project implementation agreement with the Federation and the Federation FSD (the Subsidiary Financing and Project Implementation Agreement) under terms and conditions which shall have been approved by the Association. Except as the Association shall otherwise agree, such terms and conditions shall include the following:

- (i) The Borrower shall relend to the Federation and the Federation shall relend to the Federation FSD an amount in Euro equivalent to the amount of the Credit allocated from time to time to Category A (1) set forth in the table in paragraph A.1 of Schedule 1 to this Agreement;
- (ii) The term of the Federation Subsidiary Credit shall be 35 years, including a 10-year grace period;
- (iii) The Borrower shall charge the Federation and the Federation shall charge the Federation FSD a commitment charge at a rate equal to the rate payable under Section 2.04 of this Agreement, on the principal amount of the Federation Subsidiary Credit not withdrawn from time to time;
- (iv) The Borrower shall charge the Federation a service charge on the principal amount of the Subsidiary Credit and the Federation shall charge the Federation FSD a service charge on the principal amount of the Sub-credit withdrawn and outstanding from time to time at a rate equal to the rate payable under Section 2.05 of this Agreement;

(v) The principal amount of the Subsidiary Credit and the principal amount of the Sub-credit shall be repayable in Euro and shall be the equivalent in Euro (determined as of the date or respective dates of repayment) of the value of currency or currencies withdrawn from the Credit Account on account of expenditures for the Project; and

(vi) The Borrower shall have the right to require modification in the repayment terms of the Federation Subsidiary Credit in conformity with the provisions of Section 2.07 (b) of this Agreement and the Federation shall have the right to require modification in the repayment terms of the Sub-credit in conformity with the provisions of Section 2.07 (b) of this Agreement.

(c) For the purposes of Part B of the Project, the Borrower shall enter into a subsidiary financing and project implementation agreement with Republika Srpska and the RS DEF (the Subsidiary Financing and Project Implementation Agreement) under terms and conditions which shall have been approved by the Association. Except as the Association shall otherwise agree, such terms and conditions shall include the following:

(i) The Borrower shall relend to the Republika Srpska and Republika Srpska shall relend to RS DEF an amount in Euro equivalent to the amount of the Credit allocated from time to time to Category B (1) set forth in the table in paragraph A.1 of Schedule 1 to this Agreement;

(ii) The term of the RS Subsidiary Credit and the Sub-credit, respectively, shall be 35 years, including a 10-year grace period;

(iii) The Borrower shall charge the Republika Srpska and Republika Srpska shall charge the RS DEF a commitment charge at a rate equal to the rate payable under Section 2.04 of this Agreement, on the principal amount of the RS Subsidiary Credit not withdrawn from time to time;

(iv) The Borrower shall charge the Republika Srpska a service charge on the principal amount of the Subsidiary Credit and Republika Srpska shall charge RS DEF a service charge on the principal amount of the Sub-credit withdrawn and outstanding from time to time at a rate equal to the rate payable under Section 2.05 of this Agreement;

(v) The principal amount of the Subsidiary Credit and the principal amount of the Sub-credit shall be repayable in Euro and shall be the equivalent in Euro (determined as of the date or respective dates of repayment) of the value of currency or currencies withdrawn from the Credit Account on account of expenditures for the Project; and

(vi) The Borrower shall have the right to require modification in the repayment terms of the RS Subsidiary Credit in conformity with the provisions of Section 2.07 (b) of this Agreement and Republika Srpska shall have the right to require modification in the repayment terms of the Sub-credit in conformity with the provisions of Section 2.07 (b) of this Agreement.

(d) The Borrower shall exercise its rights under the Federation Subsidiary Financing and Project Implementation Agreement and the RS Subsidiary Financing and Project Implementation Agreement in such manner as to protect the interests of the Borrower and the Association and to accomplish the purposes of the Credit, and, except as the Association shall otherwise agree, the Borrower shall not assign, amend, abrogate or waive the Federation Subsidiary Financing and Project Implementation Agreement or the RS Subsidiary Financing and Project Implementation Agreement or any provision thereof.

Section 3.02. Except as the Association shall otherwise agree, procurement of the consultants' services required for Part A of the Project and to be financed out of the proceeds of the Credit shall be governed by the provisions of Schedule 2 to the Federation Project Agreement, and procurement of the consultants' services required for Part B of the Project and to be financed out of the proceeds of the Credit shall

be governed by the provisions of Schedule 2 to the RS Project Agreement.

Section 3.03. The Borrower and the Association hereby agree that the obligations set forth in Sections 9.03, 9.04, 9.05, 9.06, 9.07 and 9.08 of the General Conditions (relating to insurance, use of goods and services, plans and schedules, records and reports, maintenance and land acquisition, respectively) in respect of Part A of the Project shall be carried out by the Federation pursuant to Section 2.05 (a) of the Federation Project Agreement and in respect of Part B of the Project shall be carried out by RS pursuant to Section 2.05 (a) of the RS Project Agreement.

#### ARTICLE IV

##### Financial Covenants

Section 4.01. (a) For all expenditures with respect to which withdrawals from the Credit Account were made on the basis of statements of expenditure, the Borrower shall:

- (i) maintain or cause to be maintained, in accordance with sound accounting practices, records and separate accounts reflecting such expenditures;
  - (ii) ensure that all records (contracts, orders, invoices, bills, receipts and other documents) evidencing such expenditures are retained until at least one year after the Association has received the audit report for the fiscal year in which the last withdrawal from the Credit Account was made; and
  - (iii) enable the Association's representatives to examine such records.
- (b) The Borrower shall:
- (i) have the records and accounts referred to in paragraph (a)(i) of this Section including and those for the Special Accounts for each fiscal year audited, in accordance with appropriate auditing principles consistently applied, by independent auditors acceptable to the Association;
  - (ii) furnish to the Association as soon as available, but in any case not later than six months after the end of each such year the report of such audit by said auditors, of such scope and in such detail as the Association shall have reasonably requested, including a separate opinion by said auditors as to whether the statements of expenditure submitted during such fiscal year, together with the procedures and internal controls involved in their preparation, can be relied upon to support the related withdrawals; and
  - (iii) furnish to the Association such other information concerning said records and accounts and the audit thereof as the Association shall from time to time reasonably request.

#### ARTICLE V

##### Remedies of the Association

Section 5.01. Pursuant to Section 6.02 (1) of the General Conditions, the following additional events are specified:

- (a) Either Entity shall have failed to perform any of its obligations under its respective Project Agreement or Subsidiary Financing and Project Implementation Agreement.
- (b) As a result of events which have occurred after the date of this Agreement, an extraordinary situation shall have arisen which shall make it improbable that either Entity shall be able to perform its obligations under its respective Project Agreement or Subsidiary Financing and Project Implementation Agreement.
- (c) The Microcredit Organization Law shall have been amended, suspended, abrogated, repealed or waived so as to affect materially and adversely the ability of the Microcredit Organizations to perform any of their obligations under the Subsidiary Credit Agreements.

(d) The Operational Guidelines shall have been amended, abrogated, repealed or otherwise modified without the prior approval of the Association.

Section 5.02. Pursuant to Section 7.01 (h) of the General Conditions, the following additional event is specified:

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

(b) the event specified in paragraph (c) of Section 5.01 of this Agreement shall occur.

## ARTICLE VI

### Effective Date; Termination

Section 6.01. The following events are specified as additional conditions to the effectiveness of this Agreement within the meaning of Section 12.01 (b) of the General Conditions:

(a) a Project Agreement has been executed on behalf of the Association and an Entity on terms and Conditions satisfactory to the Association;

(b) for the Entity referred to in paragraph (a) of this Section 6.01:

(i) the Operational Guidelines have been adopted satisfactory to the Association; and

(ii) a Subsidiary Financing and Project Implementation Agreement has been executed on behalf of the Borrower and said Entity on terms and conditions satisfactory to the Association; and

(c) the auditors referred to in Section 4.01 (b) (i) of this Agreement have been employed.

Section 6.02. The following are specified as additional matters, within the meaning of Section 12.02 (b) of the General Conditions, to be included in the opinion or opinions to be furnished to the Association:

(a) that the Project Agreement has been duly authorized or ratified by the Entity concerned and is legally binding upon said Entity in accordance with its terms; and

(b) that the Subsidiary Financing and Project Implementation Agreement referred to in Section 6.01 (b) (ii) has been duly authorized or ratified by the Borrower and said Entity and is legally binding upon the Borrower and said Entity in accordance with its terms.

Section 6.03. The date ninety (90) days after the date of this Agreement is hereby specified for the purposes of Section 12.04 of the General Conditions.

Section 6.04. The obligations of the Borrower under Article III of this Agreement shall cease and determine on the date on which the Development Credit Agreement shall terminate or on the date twenty (20) years after the date of this Agreement, whichever shall be the earlier.

## ARTICLE VII

### Representative of the Borrower; Addresses

Section 7.01. The Minister of Treasury of Institutions of Bosnia and Herzegovina and Minister of Foreign Trade and Economic Relations of Bosnia and Herzegovina are severally designated as representatives of the Borrower for the purposes of Section 11.03 of the General Conditions.

Section 7.02. The following addresses are specified for the purposes of Section 11.01 of the General Conditions:

For the Borrower:



Ministry of Treasury of Institutions of BiH  
Trg Bih 1  
71000 Sarajevo  
Bosnia and Herzegovina

For the Association:

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

Cable address:	Telex:	Facsimile:
477-6391	INDEVAS	248423 (MCI) or (202)
	Washington, D.C.	64145 (MCI)

IN WITNESS WHEREOF, the parties hereto, acting through their duly authorized representatives, have caused this Agreement to be signed in their respective names in the city of Sarajevo, Bosnia and Herzegovina, as of the day and year first above written.

BOSNIA AND HERZEGOVINA

By /s/ Azra Hadziahmetovic

Authorized Representative

INTERNATIONAL DEVELOPMENT ASSOCIATION

By /s/ Joseph Ingram

Authorized Representative

SCHEDULE 1

Withdrawal of the Proceeds of the Credit

A. General

1. The table below sets forth the Categories of items to be financed out of the proceeds of the Credit, the allocation of the amounts of the Credit to each Category and the percentage of expenditures for items so to be financed in each Category:

Category	Amount of the Credit Allocated (Expressed in SDR Equivalent)	% of Expenditures to be Financed
A. Part A of the Project (the Federation)		
(1) Microcredits	9,590,000	95% of amounts disbursed before August 31, 2002, 85% thereafter
(2) Consultants' services and training	940,000	100%
SUBTOTAL	10,530,000	

B. Part B of the Project (Republika Srpska)

(1)	Microcredits	4,800,000	95% of amounts	disbursed before August 31, 2002, 85% thereafter
(2)	Consultants' services and training	470,000	100%	
	SUBTOTAL	5,270,000		
	TOTAL	15,800,000		

2. For the purposes of this Schedule:

(a) the term "foreign expenditures" means expenditures in the currency of any country other than that of the Borrower for goods or services supplied from the territory of any country other than that of the Borrower;

(b) the term "local expenditures" means expenditures in the currency of the Borrower or for goods or services supplied from the territory of the Borrower; provided, however, that, if the currency of the Borrower is also that of another country from the territory of which goods or services are supplied, expenditures in such currency for such goods or services shall be deemed to be "foreign expenditures"; and

(c) the term "training" means training activities (other than consultants' services) to be carried out under the Project, including the cost of workshops and the travel costs and per diem of the trainees.

3. Notwithstanding the provisions of paragraph 1 above, no withdrawals shall be made in respect of: (a) payments made for expenditures prior to the date of this Agreement, except that withdrawals may be made in an aggregate amount not exceeding the equivalent of SDR 80,000, in respect of Category A (2), and SDR 40,000 in respect of Category B (2), on account of payments made for expenditures before that date but after January 1, 2001; (b) Microcredits under Categories A (1) and B (1) unless the Microcredit has been made in accordance with the criteria and procedures set forth in the Operational Guidelines and on terms and conditions referred to in the Attachment to the Annex to Schedule 1 to the Project Agreements; and (c) under the Categories allocated to Part A or Part B of the Project unless: (i) a Project Agreement between the Association and the Entity responsible for implementing Part A or Part B of the Project, as the case may be, has been executed; (ii) a Subsidiary Financing and Project Implementation Agreement has been executed with terms and conditions satisfactory to the Association; (iii) the FSD has been established in form and substance satisfactory to the Association and its Operational Guidelines have been adopted satisfactory to the Association; (iv) the financial management system referred to in Section 3.01 of the respective Project Agreement, in a format acceptable to the Association, has been established; (v) the auditors referred to in Section 4.01 (b) (i) of this Agreement have been employed; and (vi) the Association has received an opinion or opinions from counsel satisfactory to the Association that the Subsidiary Financing and Project Implementation Agreement has been duly executed by the parties thereto and is legally binding upon them in accordance with its terms.

4. The Association may require withdrawals from the Credit Account to be made on the basis of statements of expenditure for: (i) expenditures for consultants' services under contracts costing less than \$20,000 equivalent each; (ii) any amounts under contracts for training; and (iii) amounts of less than \$15,000 equivalent under Microcredits, all under such terms and conditions as the Association shall specify by notice to the Borrower.

B. Special Accounts

1. The Borrower shall open and maintain in Euro two special deposit accounts, namely the Federation Special Account and the Republika Srpska Special Account, in a commercial bank, on terms and conditions satisfactory to the Association, including appropriate protection against set-off, seizure and attachment.

2. After the Association has received evidence satisfactory to it that the Special Accounts have been opened, withdrawals from the Credit Account of amounts to be deposited into the Special Accounts shall be made as follows:

(a) until the Association shall have received: (i) the first Project Management Report referred to in Section 3.02 (b) of the Federation Project Agreement and Republika Srpska Project Agreement; and (ii) a request from the Borrower for withdrawal on the basis of Project Management Reports, withdrawals shall be made in accordance with the provisions of Annex A to this Schedule 1; and

(b) upon receipt by the Association of a Project Management Report pursuant to Section 3.02 (b) of the Federation Project Agreement and Republika Srpska Project Agreement, accompanied by a request from the Borrower for withdrawal on the basis of Project Management Reports, all further withdrawals shall be made in accordance with the provisions of Annex B to this Schedule 1.

3. Payments out of each Special Account shall be made exclusively for Eligible Expenditures. For each payment made by the Borrower out of each Special Account, the Borrower shall, at such time as the Association shall reasonably request, furnish to the Association such documents and other evidence showing that such payment was made exclusively for Eligible Expenditures.

4. Notwithstanding the provisions of Part B.2 of this Schedule, the Association shall not be required to make further deposits into any Special Account:

(a) if the Association determines at any time that any Project Management Report does not adequately provide the information required pursuant to Section 3.02 of the Project Agreements;

(b) if the Association determines at any time that all further withdrawals should be made by the Borrower directly from the Credit Account; or

(c) if the Borrower shall have failed to furnish to the Association within the period of time specified in Section 3.01 (b)(ii) of the Project Agreements, any of the audit reports required to be furnished to the Association pursuant to said Section in respect of the audit of (A) the records and accounts for any Special Account or (B) the records and accounts reflecting expenditures with respect to which withdrawals were made on the basis of Project Management Reports.

5. The Association shall not be required to make further deposits into any Special Account in accordance with the provisions of Part B.2 of this Schedule if, at any time, the Association shall have notified the Borrower of its intention to suspend in whole or in part the right of the Borrower to make withdrawals from the Credit Account pursuant to Section 6.02 of the General Conditions. Upon such notification, the Association shall determine, in its sole discretion, whether further deposits into the Special Accounts may be made and what procedures should be followed for making such deposits, and shall notify the Borrower of its determination.

6. (a) If the Association determines at any time that any payment out of any Special Account was made for an expenditure which is not an Eligible Expenditure, or was not justified by the evidence furnished to the Association, the Borrower shall, promptly upon notice from the Association, provide such additional evidence as the Association may request, or deposit into said Special Account (or, if the Association shall so request, refund to the Association) an amount equal to the amount of such payment. Unless the Association shall otherwise agree, no further deposit by the Association into any Special Account shall be made until the Borrower has provided such evidence or made such deposit or refund, as the case may be.

(b) If the Association determines at any time that any amount outstanding in any Special Account will not be required to cover payments for Eligible Expenditures during the six-month period following such determination, the Borrower shall, promptly upon notice from the Association, refund to the Association such outstanding amount.

(c) The Borrower may, upon notice to the Association, refund to the Association all or any portion of the funds on deposit in a Special Account.

(d) Refunds to the Association made pursuant to sub-paragraph (a), (b) or (c) of this paragraph 6 shall be credited to the Credit Account for subsequent withdrawal or for cancellation in accordance with the provisions of the Development Credit Agreement.

#### Annex A to SCHEDULE 1

#### Operation of Special Account When Withdrawals Are Not Made

On the Basis of Project Management Reports

1. For the purposes of this Annex:

The term "Authorized Allocation" means: (i) in respect of the Federation Special Account, an amount equivalent to Euro 1,800,000 to be withdrawn from the Credit Account and deposited into the Special Account pursuant to paragraph 2 of this Annex; provided, however, that, unless the Association shall otherwise agree, said Authorized Allocation shall be limited to an amount equivalent to Euro 900,000, until the aggregate amount of withdrawals from the Credit Account of amounts allocated to said Special Account's Eligible Categories, plus the total amount of all outstanding special commitments entered into by the Association pursuant to Section 5.02 of the General Conditions in respect of amounts allocated to said Categories, shall equal or exceed the equivalent of SDR 1,550,000; and (ii) in respect of the Republika Srpska Special Account, an amount equivalent to Euro 1,000,000 to be withdrawn from the Credit Account and deposited into the Special Account pursuant to paragraph 2 of this Annex; provided, however, that, unless the Association shall otherwise agree, said Authorized Allocation shall be limited to an amount equivalent to Euro 500,000, until the aggregate amount of withdrawals from the Loan Account of amounts allocated to said Special Account's Eligible Categories, plus the total amount of all outstanding special commitments entered into by the Association pursuant to Section 5.02 of the General Conditions in respect of amounts allocated to said Categories, shall equal or exceed the equivalent of SDR 750,000.

2. Withdrawals of a Special Account's Authorized Allocation and subsequent withdrawals to replenish said Special Account shall be made as follows:

(a) For withdrawals of said Special Account's Authorized Allocation, the Borrower shall furnish to the Association a request or requests for deposit into said Special Account of an amount or amounts which in the aggregate do not exceed said Authorized Allocation. On the basis of each such request, the Association shall, on behalf of the Borrower, withdraw from the Credit Account and deposit into said Special Account such amount as the Borrower shall have requested.

(b) For replenishment of said Special Account, the Borrower shall furnish to the Association requests for deposit into said Special Account at such intervals as the Association shall specify. Prior to or at the time of each such request, the Borrower shall furnish to the Association the documents and other evidence required pursuant to Part B.3 of Schedule 1 to this Agreement for the payment or payments in respect of which replenishment is requested. On the basis of each such request, the Association shall, on behalf of the Borrower, withdraw from the Credit Account and deposit into said Special Account such amount as the Borrower shall have requested and as shall have been shown by said documents and other evidence to have been paid out of said Special Account for Eligible Expenditures. Each such deposit into said Special Account shall be withdrawn by the Association from the Credit Account under one or more of said Special Account's Eligible Categories.

3. The Association shall not be required to make further deposits into a Special Account, once the total unwithdrawn amount of the Credit allocated to said Special Account's Eligible Categories minus the total amount of all outstanding special commitments entered into by the Association pursuant to Section 5.02 of the General Conditions in respect of expenditures to be financed out of the proceeds of the Credit allocated to said Categories, shall equal the equivalent of twice the amount of said Special Account's Authorized Allocation. Thereafter, withdrawal from the Credit Account of the remaining unwithdrawn amount of the Credit allocated to said Categories shall follow such procedures as the Association shall specify by notice to the Borrower. Such further withdrawals shall be made only after and to the extent that the Association shall have been satisfied that all such amounts remaining on deposit in said Special Account as of the date of such notice will be utilized in making payments for Eligible Expenditures.

Annex B to SCHEDULE 1

Operation of Special Account  
When Withdrawals Are Made  
On the Basis of Project Management Reports

1. Except as the Association may otherwise specify by notice to the Borrower, all withdrawals from the Credit Account shall be deposited by the Association into the respective Special Account in accordance with the provisions of Schedule 1 to this Agreement. Each such deposit into a Special Account shall be withdrawn by the Association from the Credit Account under one or more of said Special Account's

Eligible Categories.

2. Each application for withdrawal from the Credit Account for deposit into a Special Account shall be supported by a Project Management Report.

3. Upon receipt of each application for withdrawal of an amount of the Credit, the Association shall, on behalf of the Borrower, withdraw from the Credit Account and deposit into the respective Special Account an amount equal to the lesser of: (a) the amount so requested; and (b) the amount which the Association has determined, based on the Project Management Report accompanying said application, is required to be deposited in order to finance Eligible Expenditures during the six-month period following the date of such report; provided, however, that the amount so deposited, when added to the amount indicated by said Project Management Report to be remaining in said Special Account, shall not exceed the equivalent of Euro 2,500,000 in respect of the Federation Special Account and Euro 1,400,000 in respect of the Republika Srpska Special Account.

## SCHEDULE 2

### Description of the Project

The objective of the Project is to support the growth and institutional development of specialized microfinance institutions to provide financial services to low income clients in the territory of the Borrower, so as to help increase incomes, develop small businesses and create jobs.

The Project consists of the following parts, subject to such modifications thereof as the Borrower and the Association may agree upon from time to time to achieve such objectives:

#### Part A: The Federation

##### 1. Microfinance Fund

The establishment and operation of a credit facility for the financing, through the provision of Microcredits by MCOs to Sub-borrowers, of Qualifying Project Activities.

##### 2. MFI Legal and Regulatory Reform

Support for the further development of a legal and regulatory framework supportive of microfinance through provision of technical assistance and training.

##### 3. Microfinance Sector Capacity Building Support

Strengthening the capacity of MCOs through the provision of technical assistance and training so as to improve services to Sub-borrowers.

##### 4. Impact Assessment/Research and Development

Carrying out of a longitudinal impact assessment to evaluate the impacts of Microcredits on Sub-borrowers.

##### 5. Project Management

Strengthening the institutional capacity of the Federation FSD through the provision of technical assistance, training, studies, audit services, equipment, vehicles and incremental operating expenses for Project implementation.

#### Part B: Republika Srpska

##### 1. Microfinance Fund

The establishment and operation of a credit facility for the financing, through the provision of Microcredits by MCOs to Sub-borrowers, of Qualifying Project Activities.

##### 2. MFI Legal and Regulatory Reform

Support for the further development of a legal and regulatory framework supportive of microfinance through provision of technical assistance and training.

3. Microfinance Sector Capacity Building Support

Strengthening the capacity of MCOs through the provision of technical assistance and training, so as to improve services to Sub-borrowers.

4. Impact Assessment/Research and Development

Carrying out of a longitudinal impact assessment to evaluate the impacts of Microcredits on Sub-borrowers.

5. Project Management

Strengthening the institutional capacity of the RS DEF through the provision of technical assistance, training, studies, audit services, equipment, vehicles and incremental operating expenses for Project implementation.

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The Project is expected to be completed by December 31, 2004.

