

CONFORMED COPY

CREDIT NUMBER 3533 BOS

RS Project Agreement

(Second Local Initiatives (Microfinance) Project)

between

INTERNATIONAL DEVELOPMENT ASSOCIATION

and

REPUBLIKA SRPSKA

Dated October 19, 2001

CREDIT NUMBER 3533 BOS

PROJECT AGREEMENT

AGREEMENT, dated October 19, 2001 between the INTERNATIONAL DEVELOPMENT ASSOCIATION (the Association) and Republika Srpska (Republika Srpska).

WHEREAS (A) by the Development Credit Agreement of even date herewith between Bosnia and Herzegovina (the Borrower) and the Association, the Association has agreed to lend to the Borrower an amount in various currencies equivalent to fifteen million eight hundred thousand Special Drawing Rights (SDR 15,800,000), on the terms and conditions set forth in the Development Credit Agreement, but only on condition that Republika Srpska agrees to undertake such obligations toward the Association as are set forth in this Agreement; and

(B) by a subsidiary financing and project implementation agreement to be entered into among the Borrower, Republika Srpska and RS DEF (the Subsidiary Financing and Project Implementation Agreement), the Borrower will make available to Republika Srpska a portion of the proceeds of the Credit provided for under the Development Credit Agreement and Republika Srpska will make available said portion of the proceeds of the Credit to RS DEF on terms and conditions set forth in said Subsidiary Financing and Project Implementation Agreement; and

WHEREAS Republika Srpska in consideration of the Association's entering into the Development Credit Agreement with the Borrower, has agreed to undertake the obligations set forth in this Agreement;

NOW THEREFORE the parties hereto hereby agree as follows:

ARTICLE I

Definitions

Section 1.01. Unless the context otherwise requires, the several terms defined in the Development Credit Agreement, the Preamble to this Agreement and in the General Conditions (as so defined) have the respective meanings therein set forth.

ARTICLE II

Execution of Part B of the Project

Section 2.01. (a) Republika Srpska declares its commitment to the objectives of the Project as set forth in Schedule 2 to the Development Credit Agreement, and, to this end, shall cause RS DEF to carry out Part B of the Project with due diligence and efficiency and in conformity with appropriate administrative, financial, banking, environmental and technical practices, and shall provide, or cause to be provided, promptly as needed, the funds, facilities, services and other resources required for the Project.

(b) Without limitation upon the provisions of paragraph (a) of this Section and except as the Association and Republika Srpska shall otherwise agree, Republika Srpska shall cause RS DEF to carry out Part B of the Project in accordance with the Implementation Program set forth in Schedule 1 to this Agreement.

Section 2.02. Except as the Association shall otherwise agree, 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 this Agreement.

Section 2.03. Republika Srpska shall exercise its rights under the Republika Srpska Subsidiary Financing and Project Implementation Agreement in such manner as to protect the interests of Republika Srpska, the Association and the RS DEF and to accomplish the purposes of the Credit, and except as the Association shall otherwise agree, shall not assign, amend, abrogate or waive the Republika Srpska Subsidiary Financing and Project Implementation Agreement or any provision thereof.

Section 2.04. (a) Republika Srpska shall and shall cause RS DEF, at the request of the Association, to exchange views with the Association with regard to the progress of Part B of the Project, the performance of its obligations under this Agreement and under the Subsidiary Financing and Project Implementation Agreement, and other matters relating to the purposes of the Credit.

(b) Republika Srpska shall and shall cause RS DEF to promptly inform the Association of any condition which interferes or threatens to interfere with the progress of the Project, the accomplishment of the purposes of the Credit, or the performance by Republika Srpska of its obligations under this Agreement and under the Subsidiary Financing and Project Implementation Agreement.

Section 2.05. (a) Republika Srpska shall cause RS DEF to carry out 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) in respect of Part B of the Project.

(b) For the purposes of Section 9.07 of the General Conditions and without limitation thereto, RS DEF shall:

- (i) prepare, on the basis of guidelines acceptable to the Association, and furnish to the Association not later than six (6) months after the Closing Date or such later date as may be agreed for this purpose between the Association, Republika Srpska and RS DEF a plan for the future operation of Part B of the Project;
- (ii) afford the Association a reasonable opportunity to exchange views with Republika Srpska and RS DEF on said plan; and
- (iii) thereafter, carry out said plan with due diligence and efficiency and in accordance with appropriate practices, taking into account the Association's comments thereon.

ARTICLE III

Financial Covenants

Section 3.01. (a) Republika Srpska shall cause RS DEF to maintain a financial management system, including records and accounts, and prepare financial statements, in a format acceptable to the Association adequate to reflect the operations, resources and expenditures in connection with the carrying out of the Project.

(b) Republika Srpska shall cause RS DEF to:

(i) have its records, accounts and financial statements (balance sheets, statements of income and expenses and related statements) and the records and accounts 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 (6) months after the end of each such year: (A) certified copies of the financial statements referred to in paragraph (a) above for such year as so audited; and (B) the report of such audit by said auditors, of such scope and in such detail as the Association shall have reasonably requested; and

(iii) furnish to the Association such other information concerning said records and accounts and financial statements as well as the audit thereof, as the Association shall from time to time reasonably request.

Section 3.02. (a) Without limitation upon the provisions of Section 3.01 of this Agreement, Republika Srpska shall cause RS DEF to carry out a time-bound action plan acceptable to the Association for the strengthening of the financial management system referred to in paragraph (a) of said Section 3.01 in order to enable RS DEF, not later than February 15, 2002, or such later date as the Association shall agree, to prepare quarterly Project management reports, acceptable to the Association, each of which:

(i) (A) sets forth actual sources and applications of funds for the Project, both cumulatively and for the period covered by said report, and projected sources and applications of funds for the Project for the six-month period following the period covered by said report, and (B) shows separately expenditures financed out of the proceeds of the Credit during the period covered by said report and expenditures proposed to be financed out of the proceeds of the Credit during the six-month period following the period covered by said report;

(ii) (A) describes physical progress in Project implementation, both cumulatively and for the period covered by said report, and (B) explains variances between the actual and previously forecast implementation targets; and

(iii) sets forth the status of procurement under the Project and expenditures under contracts financed out of the proceeds of the Credit, as at the end of the period covered by said report.

(b) Upon the completion of the action plan referred to in paragraph (a) of this Section, RS DEF shall prepare, in accordance with guidelines acceptable to the Association, and furnish to the Association not later than forty-five (45) days after the end of each calendar quarter a Project Management Report for such period.

ARTICLE IV

Effective Date; Termination Cancellation and Suspension

Section 4.01. This Agreement shall come into force and effect on the later of: the date upon which the Development Credit Agreement becomes effective, or the date when this Agreement has been executed by the parties hereto.

Section 4.02. (a) This Agreement and all obligations of the Association and of

Republika Srpska thereunder shall terminate on the earlier of the following two dates:

- (i) the date on which the Development Credit Agreement shall terminate; or
- (ii) a date twenty (20) years after the date of this Agreement.

(b) If the Development Credit Agreement terminates before the date specified in paragraph (a) (ii) of this Section, the Association shall promptly notify Republika Srpska of this event.

Section 4.03. All the provisions of this Agreement shall continue in full force and effect notwithstanding any cancellation or suspension under the General Conditions.

ARTICLE V

Miscellaneous Provisions

Section 5.01. Any notice or request required or permitted to be given or made under this Agreement and any agreement between the parties contemplated by this Agreement shall be in writing. Such notice or request shall be deemed to have been duly given or made when it shall be delivered by hand or by mail, telegram, cable, telex or facsimile to the party to which it is required or permitted to be given or made at such party's address hereinafter specified or at such other addresses as such party shall have designated by notice to the party giving such notice or making such request. Deliveries made by facsimile transmission shall also be confirmed by mail. The addresses so specified are:

For the Association:

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

Cable address:

INTBAFRAD
Washington, D.C.

Telex:

248423 (MCI) or
64145 (MCI)

For Republika Srpska:

Ministry of Finance of Republika Srpska
Ul. Vuka Karadzica 4
78000 Banja Luka
Bosnia and Herzegovina

Section 5.02. Any action required or permitted to be taken, and any documents required or permitted to be executed, under this Agreement on behalf of Republika Srpska or by Republika Srpska on behalf of the Borrower under the Development Credit Agreement, may be taken or executed by its Minister of Finance, or by such other person or persons as Republika Srpska shall designate in writing, and Republika Srpska shall furnish to the Association sufficient evidence of the authority and the authenticated specimen signature of each such person.

Section 5.03. This Agreement may be executed in several counterparts, each of which shall be an original, and all collectively but one instrument.

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.

INTERNATIONAL DEVELOPMENT ASSOCIATION

By /s/ Joseph Ingram

Authorized Representative

REPUBLIKA SRPSKA

By /s/ Mirko Sarovic

Authorized Representative

SCHEDULE 1

Implementation Program

1. RS DEF shall maintain the Subsidiary Financing and Project Implementation Agreement and the Operational Guidelines in form and content satisfactory to the Association and Republika Srpska, shall duly perform all its obligations under the Subsidiary Financing and Project Implementation Agreement and the Operational Guidelines and shall not assign, amend, abrogate or waive the Subsidiary Financing and Project Implementation Agreement or the Operational Guidelines without obtaining the prior approval of the Association.

2. RS DEF shall:

(a) maintain policies and procedures adequate to enable it to monitor and evaluate on an ongoing basis, in accordance with the indicators agreed upon between the Borrower and the Association, the carrying out of Part B of the Project and the achievement of the objectives thereof;

(b) prepare, under terms of reference satisfactory to the Association, and furnish to the Association, on February 28 and August 31 of each year, commencing on February 28, 2002, a report integrating the results of the monitoring and evaluation activities performed pursuant to paragraph (a) of this Section, on the progress achieved in the carrying out of Part B of the Project during the twelve-month period preceding the date of said report and setting out the measures recommended to ensure the efficient carrying out of Part B of the Project and the achievement of the objectives thereof during the period following such date; and

(c) review with the Association, by March 31 and September 30 of each year during the execution of the Project, or such later date as the Association shall request, the report referred to in subparagraph (b) of this paragraph, and, thereafter, take all measures required to ensure the efficient completion of Part B of the Project and the achievement of the objectives thereof, based on the conclusions and recommendations of the said report and the Association's views on the matter.

3. For the purposes of carrying out Part B.1 of the Project, RS DEF shall:

(a) relend to the MCOs the equivalent of the proceeds of the Credit allocated from time to time to Category (B) (1) of the table set forth in paragraph 1 of Schedule 1 to the Development Credit Agreement under Subsidiary Loan Agreements to be entered into between RS DEF and each such MCO, under terms and conditions which shall have been approved by the Association, and which shall include, without limitation, those set forth in the Annex to this Schedule;

(b) monitor the overall execution of Part B.1 of the Project and the carrying out by the MCOs of their obligations under their respective Subsidiary Loan Agreements in accordance with policies and procedures satisfactory to the Association;

(c) take or cause to be taken all action necessary or appropriate on its part to enable the MCOs to perform in accordance with the provisions of their respective Subsidiary Loan Agreements all the obligations of the MCOs therein set forth, and not take or permit to be taken any action which would prevent or interfere with such performance;

(d) in respect of payment of interest or other charges on, or repayment of principal, made to it by MCOs, under the Microcredits:

- (i) open and thereafter maintain a separate account on its books in accordance with its financial procedures and on terms and conditions satisfactory to the Association;
- (ii) upon receipt of each such payment or repayment, credit the same to the said separate account;
- (iii) utilize all amounts so credited to the said separate account, to the extent they are not yet required to meet RS DEF's repayment obligations to Republika Srpska under the Subsidiary Financing and Project Implementation Agreement, exclusively to finance its operating costs acceptable to the Association and other microcredit lending activities in accordance with the terms and conditions of this Schedule 1 and the Operational Guidelines; and
- (iv) prepare and furnish to the Association at regular intervals all such information, in form and substance satisfactory to the Association, on the status of said separate account and on the utilization of the amounts credited thereto; and

(e) exercise its rights under the Subsidiary Loan Agreements in such manner as to protect the interests of the Association, the Borrower and Republika Srpska and to accomplish the purposes of the Credit, and, except as the Association shall otherwise agree, not assign, amend, abrogate or waive any such Agreement or any provision thereof.

ANNEX TO SCHEDULE 1

Principal Terms and Conditions of the Subsidiary Loan Agreements

The principal terms and conditions set forth in this Schedule shall apply for the purposes of paragraph 4 (a) of Schedule 1 to this Agreement.

A. Terms

1. The principal amount to be relented out of the proceeds of the Credit to a MCO under its respective Subsidiary Loan Agreement shall be denominated in Euro and be the equivalent of the aggregate amount of the principal of all Microcredits made out of the proceeds thereof.

2. The Subsidiary Loan shall: (i) be charged monthly, on the principal amount thereof withdrawn and outstanding from time to time, interest at a rate equal to the cost of IDA funds plus an interest spread, not to exceed five percent (5%) per annum, to cover the reasonable costs of administering Microcredits; such interest rate shall be reviewed by the parties semi-annually; (ii) have a maturity of not more than fifteen (15) years; (iii) be repaid, in respect of interest, monthly; and (iv) be repaid, in respect of principal, semi-annually commencing five years after the date of the Subsidiary Loan Agreement.

3. The right of a MCO to the use of the proceeds of its respective Subsidiary Loan shall be: (a) suspended upon failure of such MCO to perform any of its obligations under its respective Subsidiary Loan Agreement or to continue to be in compliance with all legal and regulatory requirements applicable to its operations; and (b) terminated if such right shall have been suspended pursuant to subparagraph (a) hereof for a continuous period of sixty (60) days.

B. Conditions

1. A Subsidiary Loan Agreement may be entered into with a MCO, which RS DEF shall have determined, and the Association shall have agreed, that such MCO:

- (a) is duly established and licensed to operate in Republika Srpska;
- (b) has in place a managerial capacity under independent oversight acceptable to the Association;
- (c) has a sound and balanced credit risk management program acceptable to the Association;

(d) is operating pursuant to investment and lending policies and procedures acceptable to the Association, and has undertaken to maintain said policies and procedures;

(e) is in compliance with the Microcredit Organization Law and other applicable laws and regulations of Republika Srpska; and

(f) conforms to other eligibility criteria that shall have been adopted for the purposes of the Project acceptable to the Association.

2. Each respective Subsidiary Loan Agreement shall contain provisions pursuant to which each respective MCO shall undertake to:

(a) carry out activities under Part B.1 of the Project and conduct its operations and affairs in accordance with appropriate financial standards and practices, with qualified management and staff in adequate numbers, and in conformity with the investment and lending policies and procedures referred to in paragraph 1 (c) hereof;

(b) (i) make Microcredits to Sub-borrowers on the terms and conditions set forth in the Operational Guidelines including, without limitation, the terms and conditions set forth in the Attachment to this Annex;

(ii) exercise its rights in relation to each such Microcredit in such manner as to protect its interests and the interests of the Borrower, Republika Srpska and the Association, comply with its obligations under its respective Subsidiary Loan Agreement and achieve the purposes of Part B.1 of the Project;

(iii) not assign, amend, abrogate or waive any of its agreements providing for Microcredits, or any provision thereof, without prior approval of Republika Srpska; and

(iv) appraise Qualifying Project Activities and supervise, monitor and report on the carrying out by the Sub-borrowers of Qualifying Project Activities, in accordance with the Operational Guidelines;

(c) (i) exchange views with, and furnish all such information to the Association or RS DEF, as may be reasonably requested by the Association, Republika Srpska or the RS DEF, with regard to the progress of its activities under Part B.1 of the Project, the performance of its obligations under its respective Subsidiary Loan Agreement, and other matters relating to the purposes of Part B.1 of the Project;

(ii) prepare and submit to RS DEF quarterly reports on Microcredit disbursements and repayments; and

(iii) promptly inform the Association and RS DEF of any condition which interferes or threatens to interfere with the progress of its activities under its respective Subsidiary Loan Agreement; and

(d) (i) maintain records and accounts adequate to reflect, in accordance with sound accounting practices, its operations and financial condition; and

(ii) furnish to the Association such information concerning said records and accounts as the Association shall from time to time reasonably request.

ATTACHMENT TO THE ANNEX TO SCHEDULE 1

Terms and Conditions of the Microcredits

The provisions of this Attachment shall be for the purposes of paragraph 2 (b) (i) of Part B of the Annex to this Schedule 1.

1. The principal amount of each Microcredit made out of the proceeds of the Credit allocated from time to time to Category (B) (1) of the table set forth in paragraph 1 of Schedule 1 to the Development Credit Agreement shall:

(a) be denominated in KM, and be the equivalent in KM (determined as of the date or respective dates of withdrawal from the Credit Account or payment out of the Special Account) of the value of the currency or currencies so withdrawn or paid out on account of the cost of goods and services financed out of such proceeds for Microcredits under Part B.3 of the Project; and

(b) unless otherwise agreed by the Association, not exceed the equivalent of KM 30,000, provided, however, that the amount of the initial Microcredit by an MCO to any Sub-borrower shall not exceed KM 5,000.

2. Each Microcredit shall:

(a) bear interest on the principal amount thereof withdrawn and outstanding from time to time, at a rate determined by the MCO, sufficient to cover the full costs of lending, including administration costs, costs of capital, expected loan losses, and inflation, and take into account positive real interest rates prevailing in the Borrower's financial markets;

(b) be repaid, in respect of interest on the outstanding principal balance of the Microcredit, monthly, as determined by the MCO in accordance with its investment and lending policies; and

(c) be repaid, in respect of the principal balance of the Microcredit disbursed and outstanding, within a period of three (3) years or less.

3. Microcredits shall be made to Sub-borrowers each of which shall have established, to the satisfaction of the MCO making the Microcredit, on the basis of the MCO's Operational Guidelines in conformity with the eligibility criteria for Sub-borrowers acceptable to the Association.

4. Microcredits shall be made for Qualifying Project Activities which are each determined, on the basis of an appraisal carried out in accordance with the MCO's Operational Guidelines, conformity to eligibility criteria for Qualifying Project Activities acceptable to the Association.

5. Microcredits shall be made on terms whereby the MCO making the Microcredit shall obtain, by written contract or other appropriate means, rights adequate to protect its interest and those of RS DEF, Republika Srpska and the Association, including the right to:

(a) require the Sub-borrower to carry out the Qualifying Project Activity in conformity with appropriate practices, to maintain adequate records, and to provide, promptly as needed, the funds, facilities and other resources required for the purpose;

(b) require that: (i) the works, goods and consultants' services to be financed out of the proceeds of the Credit shall be procured using purchasing practices, which usually involves comparing more than one price quotation; and (ii) such goods and services be used exclusively in the carrying out of the Qualifying Project Activity;

(c) inspect, by itself or jointly with representatives of the Association or RS DEF, if the Association, Republika Srpska or RS DEF shall so request, the goods and the sites, works, plans and construction included in the Qualifying Project Activity, the operation thereof, and any relevant records and documents;

(d) carry out and operate the Qualifying Project Activity in accordance with appropriate health, safety and environmental standards, satisfactory to the Association; and

(e) suspend or terminate the right of the Sub-borrower to the use of the proceeds of the Credit upon failure by such Sub-borrower to perform its obligations under its contract with the MCO.

SCHEDULE 2

Procurement and Consultants' Services

Section I. Employment of Consultants

Part A: General

Consultants' services shall be procured in accordance with the provisions of the Introduction and Section IV of the "Guidelines: Selection and Employment of Consultants by World Bank Borrowers" published by the Bank in January 1997 and revised in September 1997 and January 1999 (the Consultant Guidelines) and the following provisions of Section II of this Schedule.

Part B: Quality- and Cost-based Selection

1. Consultants' services shall be procured under contracts awarded in accordance with the provisions of Section II of the Consultant Guidelines, paragraph 3 of Appendix 1 thereto, Appendix 2 thereto, and the provisions of paragraphs 3.13 through 3.18 thereof applicable to quality- and cost-based selection of consultants.

2. The following provisions shall apply to consultants' services to be procured under contracts awarded in accordance with the provisions of the preceding paragraph. The short list of consultants for services under Part B.1 and 2 of the Project, estimated to cost less than \$200,000 equivalent per contract, may comprise entirely national consultants in accordance with the provisions of paragraph 2.7 of the Consultant Guidelines.

Part C: Other Procedures for the Selection of Consultants

1. Selection Based on Consultants' Qualifications

Services for technical assistance and training assignments under Part B.2 of the Project, estimated to cost less than \$100,000 equivalent per contract, up to an aggregate amount not to exceed \$137,000, may be procured under contracts awarded in accordance with the provisions of paragraphs 3.1 and 3.7 of the Consultant Guidelines.

2. Single Source Selection

Services for impact assessment advice and research under Part B.2 of the Project, up to an aggregate amount not to exceed \$42,000 equivalent, may, with the Association's prior agreement, be procured in accordance with the provisions of paragraphs 3.8 through 3.11 of the Consultant Guidelines.

3. Individual Consultants

Services that meet the requirements set forth in paragraph 5.01 of the Consultant Guidelines, up to an aggregate amount not to exceed \$160,000 equivalent, shall be procured under contracts awarded to individual consultants in accordance with the provisions of paragraphs 5.1 through 5.3 of the Consultant Guidelines.

Part D: Review by the Association of the Selection of Consultants

1. Selection Planning

Prior to the issuance to consultants of any requests for proposals, the proposed plan for the selection of consultants under the Project shall be furnished to the Association for its review and approval, in accordance with the provisions of paragraph 1 of Appendix 1 to the Consultant Guidelines. Selection of all consultants' services shall be undertaken in accordance with such selection plan as shall have been approved by the Association, and with the provisions of said paragraph 1.

2. Prior Review

(a) With respect to each contract for the employment of consulting firms estimated to cost the equivalent of \$25,000 or more, the procedures set forth in paragraphs 1, 2 and (other than the third subparagraph of paragraph 2 (a)) and 5 of Appendix 1 to the Consultant Guidelines shall apply.

(b) With respect to each contract for the employment of individual consultants estimated to cost the equivalent of \$25,000 or more, the qualifications, experience, terms of reference and terms of employment of the consultants shall be furnished to the Association for its prior review and approval. The contract shall be awarded only after the said approval shall have been given.

3. Post Review

With respect to each contract not governed by paragraph 2 of this Part, the procedures set forth in paragraph 4 of Appendix 1 to the Consultant Guidelines shall apply.

