

CONFORMED COPY

CREDIT NUMBER 3191 BOS

Development Credit Agreement

(Local Development Pilot Project)

between

BOSNIA AND HERZEGOVINA

and

INTERNATIONAL DEVELOPMENT ASSOCIATION

Dated as of June 3, 1999

CREDIT NUMBER 3191 BOS

DEVELOPMENT CREDIT AGREEMENT

AGREEMENT, dated as of June 3, 1999, between BOSNIA and HERZEGOVINA (the Borrower) and the 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; and

(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 the RS a part of the proceeds of the Credit as provided in this Agreement; and

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 December 2, 1997, 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 10 of Resolution No. 183 of the Board of Governors of the Association, adopted on June 26, 1996; and 'Participating Countries' means, collectively, all such countries.

(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: (i) 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 (ii) 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) "Deutsche Mark" and "DEM" each mean the lawful currency of the Federal Republic of Germany;

(b) "Eligible Categories" means, in respect of the Federation Special Account for Part A of the Project, Categories A (1), (2), (3) and (4) 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 (5), (6), (7) and (8) set forth in said table;

(c) "Eligible Expenditures" means, in respect of the Federation Special Account for Part A of the Project, the expenditures for goods, works and services referred to in Section 2.02 of this Agreement 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 expenditures for goods, works and services referred to in Section 2.02 of this Agreement 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 or Republika Srpska, as the case may be, and "Entities" means the Federation and Republika Srpska, collectively;

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

(f) "Federation LDF" means the Federation Local Development Fund, a legal entity, established or to be established under the laws of the Federation and includes any successor thereto acceptable to the Association;

(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) "Federation Subsidiary Financing and Project Implementation Agreement" means the tripartite agreement entered or to be entered into between the Borrower, the Federation and the Federation LDF pursuant to Section 3.01 (b) of this Agreement, as the same may be amended from time to time, and such term includes all schedules to the Federation Subsidiary Financing and Project Implementation Agreement, and "Federation

Subsidiary Credit" means the credit provided under the Federation Subsidiary Financing and Project Implementation Agreement;

(i) "KM" or "Konvertibilna Marka" means the lawful currency of the Borrower;

(j) "Operational Guidelines" means the guidelines to be adopted by the Federation LDF and RS LDF, pursuant to Section 6.01 (b) (i) and paragraph A.3 (c) (iii) of Schedule 1 to this Agreement, setting out the operational and administrative procedures for the implementation of the Project including the preparation, approval, processing, financing, implementation and supervision of Sub-loans;

(k) "Participating Financial Institution" or "PFI" means any private or to be privatized commercial bank registered according to the applicable laws and regulations of the Federation or Republika Srpska (defined hereinafter), in which the management is not directly or indirectly controlled by the Federation or Republika Srpska, and more than fifty percent (50%) of the shareholding is held by persons or entities other than the Federation or Republika Srpska, the local authorities or any subdivision thereof, or entities controlled by the Federation or Republika Srpska, and selected pursuant to criteria set forth in paragraph B.1 of Annex to Schedule 1 to the Project Agreements (defined hereafter);

(l) "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;

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

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

(o) "RS LDF" means the RS Local Development Fund, a legal entity established or to be established under the laws of Republika Srpska and includes any successor thereto acceptable to the Association;

(p) "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;

(q) "RS Subsidiary Financing and Project Implementation Agreement" means the tripartite agreement entered or to be entered into between the Borrower, Republika Srpska, and RS LDF pursuant to Section 3.01 (c) of this Agreement, as the same may be amended from time to time, and such term includes all schedules to the RS Subsidiary Financing and Project Implementation Agreement, and "RS Subsidiary Credit" means the credit provided under the RS Subsidiary Financing and Project Implementation Agreement;

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

(s) "Sub-borrower" means a municipality or city of the Federation or Republika Srpska, other than Brcko, or an entity operating a public service, as the case may be, selected pursuant to criteria set forth in paragraph 5 of the Attachment to the Annex to Schedule 1 to Project Agreements, to which a PFI (defined hereafter) proposes to make or has made a Sub-loan (defined hereafter);

(t) "Sub-loan" means a loan made or proposed to be made by a PFI out of the proceeds of the Credit to a Sub-borrower for a Sub-project (defined hereafter);

(u) "Sub-project" means a specific development project to be carried out by a Sub-borrower utilizing the proceeds of a Sub-loan;

(v) "Subsidiary Financing and Project Implementation Agreement" means either agreement entered or to be entered into between the Borrower, each Entity and respective LDF pursuant to Section 3.01 (b) or (c) of this Agreement, as the same agreement may be amended from time to time, and such term includes all schedules supplemental to each Subsidiary Financing and Project Implementation Agreement; "Subsidiary Financing and Project Implementation Agreements" means said agreements, collectively; "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 out of the proceeds of the Subsidiary Credit provided to each LDF under a Subsidiary Financing and Project Implementation Agreement;

(w) "Subsidiary Loan" means any loan made pursuant to a Subsidiary Loan Agreement (defined hereafter); and

(x) "Subsidiary Loan Agreement" means any agreement entered or to be entered into between the Federation LDF or RS LDF and a PFI pursuant to paragraph B.2 of Annex to Schedule 1 to the 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 eleven million one hundred thousand Special Drawing Rights (SDR 11,100,000).

Section 2.02. 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 goods and 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 a PFI on account of withdrawals made by a Sub-borrower under a Sub-loan to meet the reasonable cost of goods, works and services required for the Sub-project under Part A.3 and B.3 of the Project in respect of which the withdrawal from the Credit Account is requested.

Section 2.03. The Closing Date shall be May 31, 2003, 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 (60) days after the date of this Agreement (the accrual date) to the respective dates on which amounts shall be withdrawn by the Borrower from the Credit Account or cancelled; and (ii) at the rate set as of 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 1 and October 1 in each year.

Section 2.07. (a) Subject to paragraphs (b) and (c) below, the Borrower shall repay the principal amount of the Credit in semi-annual installments payable on each April 1 and October 1 commencing October 1, 2009, and ending April 1, 2034. Each installment to and including the installment payable on April 1, 2019, 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 (3) 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 semi-annual payment date referred to in paragraph (a) above falling six (6) 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 (5) years on such repayment of principal.

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

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

Section 2.08. The currency of the United States of America is hereby specified for the purposes of Section 4.02 of the General Conditions.

### ARTICLE III

#### 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 LDF (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 LDF an amount in Dollars equivalent to the amount of the Credit allocated from time to time to Categories A (1), (2), (3) and (4) set forth in the table in paragraph A.1 of Schedule 1 to this Agreement;
- (ii) the term of the Federation Subsidiary Credit and the Sub-credit, respectively, shall be 35 years, including a 10-year grace period;
- (iii) the Borrower shall charge the Federation and the Federation shall charge the Federation LDF 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 LDF 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 Dollars and shall be the equivalent in Dollars (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 LDF (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 Republika Srpska and Republika Srpska shall relend to RS LDF an amount in Dollars equivalent to the amount of the Credit allocated from time to time to Categories B (5), (6), (7) and (8) 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 Republika Srpska and Republika Srpska shall charge the RS LDF 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 Republika Srpska a service charge on the principal amount of the Subsidiary Credit and Republika Srpska shall charge RS LDF 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 Dollars and shall be the equivalent in Dollars (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 if 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, 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 goods, works, and 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 goods, works and

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 LDF 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 LDF 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 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 (1) 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 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 (6) 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) the Federation LDF or the RS LDF shall have failed to perform any of its obligations under its respective Subsidiary Financing and Project Implementation Agreement;

(c) 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;

(d) 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 the Federation LDF or the RS LDF shall be able to perform its obligations under its respective Subsidiary Financing and Project Implementation Agreement;

(e) the Operational Guidelines shall have been amended, abrogated, repealed or otherwise modified without the prior approval of the Association; and

(f) the founding documents of the Federation LDF or the RS LDF shall have been amended, suspended, abrogated, repealed or waived so as to affect materially and adversely the operations or financial condition of the Federation LDF or RS LDF or its ability to carry out its respective part of the Project or to perform any of its respective obligations under the Federation Subsidiary Financing and Project Implementation Agreement and Republika Srpska Subsidiary Financing and Project Implementation Agreement.

Section 5.02. Pursuant to Section 7.01 (h) of the general Conditions, the following additional events are specified:

(a) the events specified in paragraphs (a), (b) and (e) 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) any event specified in paragraph (f) 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 paragraph (a) of this Section 6.01:

(i) the respective LDF has been established in form and substance satisfactory to the Association and its Operational Guidelines have been adopted satisfactory to the Association;

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

(iii) 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; 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, with the meaning of Section 12.02 (c) 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 on 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 and is legally binding upon the Borrower, said Entity and the respective LDF 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 Foreign Trade and Economic Relations of the Borrower is designated as the representative 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 Foreign Trade  
and Economic Relations  
Musala 9  
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:

INTBAFRAD  
Washington, D.C.

Telex:

248423 (MCI)  
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/ Zivko Radisic

Authorized Representative

INTERNATIONAL DEVELOPMENT ASSOCIATION

By /s/ Rory O'Sullivan

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) Sub-loans	6,120,000	100% (of amounts disbursed)
(2) Goods	50,000	100% of foreign expenditures, 100% of local expenditures (ex-factory cost) and 85% of local expenditures for other items procured locally
(3) Consultants' services, training and auditing	1,240,000	100%
(4) Incremental operating costs	250,000	90% up to \$260,000 and 75% thereafter
SUB-TOTAL	7,660,000	
B. Part B of the Project (Republika Srpska)		
(5) Sub-loans	2,640,000	100% (of amounts disbursed)
(6) Goods	20,000	100% of foreign expenditures, 100% of local expenditures (ex-factory cost) and 85% of local expenditures for other items procured locally
(7) Consultants' services, training and auditing	530,000	100%
(8) Incremental operating costs	250,000	90% up to \$260,000 and 75% thereafter
SUB-TOTAL	3,440,000	
TOTAL	11,100,000	

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";

(c) the term "incremental operating costs" means the incremental expenses incurred by the Federation LDF or RS LDF on account of Project implementation, management and monitoring, including staff salaries, office supplies, vehicle operation, travel; and

(d) 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 cost and per diem of the trainees.

3. Notwithstanding the provisions of paragraph 1 above, no withdrawals shall be made in respect of payments made for expenditures: (a) prior to the date of this Agreement; (b) under Categories A (1) and B (1) unless the Sub-loan 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 between the Borrower, such Entity and the respective LDF has been executed with terms and conditions satisfactory to the Association; (iii) the respective LDF 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) an opinion has been furnished to the Association stating that such Project Agreement and Subsidiary Financing and Project Implementation Agreement have been duly authorized or ratified 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: (a) contracts for employment of consulting firms not exceeding \$100,000 equivalent; (b) incremental operating costs; and (c) contracts for employment of individual consultants not exceeding \$20,000 equivalent, each 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 DEM 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 Project Management Reports 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 the 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 this 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:

(a) the term "Authorized Allocation" means: (i) in respect of the Federation Special Account for Part A of the Project, an amount equivalent to DEM 1,780,000 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 DEM 890,000, 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 1,100,000; and (ii) in respect of the Republika Srpska Special Account for Part B of the Project, an amount equivalent to DEM 890,000 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 Authorization Allocation shall be limited to an amount equivalent to DEM 440,000, 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 510,000.

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 said 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 the said Special Account's Authorized Allocation. Thereafter, withdrawal from the Credit Account of the remaining unwithdrawn amount of the Credit 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 this 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 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 DEM 3,550,000 in respect of the Federation Special Account for Part A of the Project and DEM 1,780,000 in respect of Republika Srpska Special Account for Part B of the Project.

#### SCHEDULE 2

##### Description of the Project

The objectives of the Project are to: (a) strengthen the institutional and financial capacity of local governments to provide improved infrastructure and services and to help stimulate local economic growth; and (b) initiate, on a pilot basis, the development of a credit market for municipal investment.

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. Local Government Capacity Building

Strengthening the capacity of Sub-borrowers through the provision of technical assistance and training to carry out Sub-projects.

2. Banking Sector Capacity Building

Strengthening the capacity of PFIs through the provision of technical assistance and training to improve municipal credit analysis and lending skills.

3. Local Development Fund

The establishment and operation of a credit facility for the financing, through the provision of Sub-loans by PFIs to Sub-borrowers, of Sub-projects.

4. Project Management

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

Part B: Republika Srpska

1. Local Government Capacity Building

Strengthening the capacity of Sub-borrowers through the provision of technical assistance and training to carry out Sub-projects.

2. Banking Sector Capacity Building

Strengthening the capacity of PFIs through the provision of technical assistance and training to improve municipal credit analysis and lending skills.

3. Local Development Fund

The establishment and operation of a credit facility for the financing, through the provision of Sub-loans by PFIs to Sub-borrowers, of Sub-projects.

4. Project Management

Strengthening the institutional capacity of RS LDF 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 November 30, 2002.

