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FINANCING NUMBER H217-LA

Financing Agreement

(Second Poverty Reduction Support Operation/Program)

between

LAO PEOPLE'S DEMOCRATIC REPUBLIC

and

INTERNATIONAL DEVELOPMENT ASSOCIATION

Dated June 2, 2006

FINANCING NUMBER H217-LA

FINANCING AGREEMENT

Agreement dated June 2, 2006, entered into between LAO PEOPLE'S DEMOCRATIC REPUBLIC ("Recipient") and INTERNATIONAL DEVELOPMENT ASSOCIATION ("Association") for the purpose of providing financing in support of the Program (as defined in the Appendix to this Agreement). The Association has decided to provide this financing on the basis, inter alia, of the Recipient's maintenance of an appropriate macro-economic policy framework. The Recipient and the Association therefore hereby agree as follows:

ARTICLE I – GENERAL CONDITIONS; DEFINITIONS

- 1.01. The General Conditions (as defined in the Appendix to this Agreement) constitute an integral part of this Agreement.
- 1.02. Unless the context requires otherwise, the capitalized terms used in the Financing Agreement have the meanings ascribed to them in the General Conditions or in the Appendix to this Agreement.

ARTICLE II – FINANCING

- 2.01. The Association agrees to extend to the Recipient, on the terms and conditions set forth or referred to in this Agreement, a grant in an amount equivalent to five million six hundred thousand Special Drawing Rights (SDR 5,600,000) ("Grant");
- 2.02. The Recipient may withdraw the proceeds of the Financing in support of the Program in accordance with Section II of Schedule 1 to this Agreement.
- 2.03. The Maximum Commitment Charge Rate payable by the Recipient on the Unwithdrawn Financing Balance shall be one-half of one percent (1/2 of 1%) per annum.
- 2.04. The Payment Dates are April 1 and October 1 in each year.

2.05. The Payment Currency is United States dollars.

ARTICLE III – PROGRAM

- 3.01. The Recipient declares its commitment to the Program and its implementation. To this end:
- (a) the Recipient and the Association shall from time to time, at the request of either party, exchange views on the progress achieved in carrying out the Program;
 - (b) prior to each such exchange of views, the Recipient shall furnish to the Association for its review and comment a report on the progress achieved in carrying out the Program, in such detail as the Association shall reasonably request; and
 - (c) without limitation upon the provisions of paragraphs (a) and (b) of this Section, the Recipient shall exchange views with the Association on any proposed action to be taken after the disbursement of the Financing which would have the effect of materially reversing the objectives of the Program, or any action taken under the Program including any action specified in Section I of Schedule 1 to this Agreement.

ARTICLE IV – REMEDIES OF THE ASSOCIATION

4.01. The Additional Event of Suspension consists of the following, normally a situation has arisen which shall make it improbable that the Program, or a significant part of it, will be carried out.

ARTICLE V – EFFECTIVENESS

5.01. The Effectiveness Deadline is the date ninety (90) days after the date of this Agreement.

ARTICLE VI – REPRESENTATIVE; ADDRESSES

6.01. The Recipient's Representative is the Recipient's Minister of Finance.

6.02. The Recipient's Address is:

Ministry of Finance
Post Box No. 46
Vientiane
Lao PDR

Facsimile: 856-21-412142

6.03. The Association's Address is:

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

Cable address:	Telex:	Facsimile:
INDEVAS Washington, D.C.	248423(MCI) or 64145(MCI)	1-202-477-6391

AGREED at Vientiane, Lao People's Democratic Republic, as of the day and year first above written.

LAO PEOPLE'S DEMOCRATIC REPUBLIC

By /s/ Somdy Douangdy

Authorized Representative

INTERNATIONAL DEVELOPMENT ASSOCIATION

By /s/ Ian Porter

Authorized Representative

SCHEDULE 1

Program Actions; Availability of Financing Proceeds

Section I. Actions Taken Under the Program

The actions taken by the Recipient under the Program include the following:

1. The MOF has approved the Public Expenditure Management Strengthening Program's annual implementation plan and the capacity building plan for FY 2005-06.
2. The MOF has prepared its FY 2005-06 budget with administrative classifications, priority expenditure sectors, and summary data on statutory funds.
3. The MOF has initiated a program to develop a new, Government Financial Statistics-compatible chart of accounts, a new budget nomenclature, and a strategy for implementation.
4. The MOF has maintained and monitored records for central administration and selected provinces of: (a) accounts payable; and (b) treasury balances; and has prepared cash plans for central administration.
5. The Recipient has launched independent external audits of financial accounts for FY 2004 for Lao Airlines (LA), Nam Papa Lao (NPNL), Pharmaceutical Factory 3 (PH3) and Bolisat Pattana Khet Poudoi (BPKP).
6. The Recipient has approved for restructuring and initiated preparation of restructuring plans for four (4) of the fourteen (14) non-performing State Owned Enterprises identified in the State Asset Management Department's 2003 assessment: Lane Xang Phatthana (LXP); Lat Visahakit Sanong Vatthou Technique (LVSVT); Lat Visahakit Konchak Kasikam (LVKK); and Bolisat Phalithaphanh Beton Lao (BPBL) (PMO Notice No. 1941 of December 22, 2005).
7. The Recipient has adopted the action plan for financial sustainability of the power sector, to ensure continued financial viability of *Electricité du Laos*.
8. The Recipient has paid the salaries of health care workers such that the stock of salaries outstanding more than one (1) month came below twenty-two percent (22%) of a month's payroll.

9. The Recipient has paid the salaries of teachers such that the stock of salaries outstanding more than one (1) month came below six percent (6%) of a month's payroll.

10. The Recipient's National Assembly has approved the new Enterprise Law, replacing the 1994 Business Law.

Section II. Availability of Financing Proceeds

A. General. The Recipient may withdraw the proceeds of the Financing in accordance with the provisions of this Section and such additional instructions as the Association may specify by notice to the Recipient.

B. Allocation of Financing Amounts. The Financing shall be withdrawn in a single tranche. The allocation of the amounts of the Financing to this end is set out in the table below:

Allocations	Amount of the Financing Allocated (expressed in SDRs)
Single Tranche	SDR 5,600,000
TOTAL AMOUNT	SDR 5,600,000

C. Deposits of Financing Amounts. Except as the Association may otherwise agree:

1. all withdrawals from the Financing Account shall be deposited by the Association into an account designated by the Recipient and acceptable to the Association; and
2. the Recipient shall ensure that upon each deposit of an amount of the Financing into this account, an equivalent amount is accounted for in the Recipient's budget management system, in a manner acceptable to the Association.

D. Excluded Expenditures. The Recipient undertakes that the proceeds of the Financing shall not be used to finance Excluded Expenditures. If the Association determines at any time that an amount of the Financing was used to make a payment for an Excluded Expenditure, the Recipient shall, promptly upon notice from the Association, refund an amount equal to the amount of such

payment to the Association. Amounts refunded to the Association upon such request shall be cancelled.

E. Audit. Upon the Association's request, the Recipient shall:

1. have the account referred to in Part C. 1 of Section II of Schedule 1 to this Agreement audited by independent auditors acceptable to the Association, in accordance with consistently applied auditing standards acceptable to the Association;
2. furnish to the Association as soon as available, but in any case not later than four (4) months after the date of the Association's request for such audit, a certified copy of the report of such audit, of such scope and in such detail as the Association shall reasonably request; and
3. furnish to the Association such other information concerning the said account and their audit as the Association shall reasonably request.

F. Closing Date. The Closing Date is February 28, 2007.

APPENDIX

Section I. Definitions

1. “Bolisat Pattana Khet Pudoi” means a wholly state-owned enterprise established and operating pursuant to Decree No. 188, dated August 19, 1984, and any successor thereto.
2. “Bolisat Phalithaphanh Beton Lao” means a wholly state-owned enterprise established and operating pursuant to Decree No. 136 dated August 10, 1998, of the Recipient’s Ministry of Industry and Handicraft, and any successor thereto.
3. “Excluded Expenditure” means any expenditure:
 - (a) for goods or services supplied under a contract which any national or international financing institution or agency other than the Association or the Bank has financed or agreed to finance, or which the Association or the Bank has financed or agreed to finance under another Financing, credit, grant or loan;
 - (b) for goods included in the following groups or sub-groups of the Standard International Trade Classification, Revision 3 (SITC, Rev.3), published by the United Nations in Statistical Papers, Series M, No. 34/Rev.3 (1986) (the SITC), or any successor groups or sub-groups under future revisions to the SITC, as designated by the Association by notice to the Recipient:

Group	Sub-group	Description of Item
112		Alcoholic beverages
121		Tobacco, un-manufactured, tobacco refuse
122		Tobacco, manufactured (whether or not containing tobacco substitutes)
525		Radioactive and associated materials
667		Pearls, precious and semiprecious stones, unworked or worked
718	718.7	Nuclear reactors, and parts thereof; fuel elements (cartridges), non-irradiated, for nuclear reactors

Group	Sub-group	Description of Item
728	728.43	Tobacco processing machinery
897	897.3	Jewelry of gold, silver or platinum group metals (except watches and watch cases) and goldsmiths' or silversmiths' wares (including set gems)
971		Gold, non-monetary (excluding gold ores and concentrates)

- (c) for goods intended for a military or paramilitary purpose or for luxury consumption;
 - (d) for environmentally hazardous goods, the manufacture, use or import of which is prohibited under the laws of the Recipient or international agreements to which the Recipient is a party;
 - (e) on account of any payment prohibited by a decision of the United Nations Security Council taken under Chapter VII of the Charter of the United Nations; and
 - (f) under a contract with respect to which the Association determines that corrupt, fraudulent, collusive or coercive practices were engaged in by representatives of the Recipient or other recipient of the Financing proceeds during the procurement or execution of such contract, without the Recipient (or other such recipient) having taken timely and appropriate action satisfactory to the Association to remedy the situation.
4. "FY" means: (a) in the case of the Recipient, the fiscal year extending from October 1 in any calendar year through September 30 of the following year; and (b) in the case of Lao Airlines, Nam Papa Lao, Pharmaceutical Factory 3, and Bolisat Pattana Khet Poudoi, the fiscal year extending from January 1 to December 31.
5. "General Conditions" means the "International Development Association General Conditions for Credit and Grants", dated July 1, 2005, with the modifications set forth in Section II of this Appendix.

6. “Lane Xang Phatthana” means a wholly state-owned enterprise established and operating pursuant to Decree No. 0798/CPMO dated May 11, 1999, of the Recipient’s Ministry of Commerce and any successor thereto.
7. “Lat Visahakit Konchak Kasikam” means a wholly state-owned enterprise established and operating pursuant to Decree No. 985/CPMO dated June 21, 1997, of the Recipient’s Ministry of Agriculture-Forest, and any successor thereto.
8. “Lat Visahakit Sanong Vatthou Technique” means a wholly state-owned enterprise established and operating pursuant to Decree No. 360/MOC dated September 4, 1983, of the Recipient’s Ministry of Commerce and any successor thereto.
9. “Lao Airlines” means the wholly state-owned enterprise established and operating pursuant to Decision No. 771/MCTPC dated May 23, 1989, of the Recipient’s Ministry of Communication, Transport, Post and Construction, and any successor thereto.
10. “MOF” means the Recipient’s Ministry of Finance or any successor thereto.
11. “Nam Papa Laos” means a wholly state-owned enterprise established and operating pursuant to Decision No. 1296, dated April 5, 2001, of the Recipient’s Ministry of Transport and Communications, and any successor thereto.
12. “Pharmaceutical Factory 3” means a wholly state-owned enterprise established and operating pursuant to Resolution No. 275, dated May 15, 1987, of the Recipient’s Ministry of Health, and any successor thereto.
13. “Program” means the program of actions, objectives and policies designed to promote growth and achieve sustainable reductions in poverty and set forth or referred to in the letter dated March 17, 2006, from the Recipient to the Association declaring the Recipient’s commitment to the execution of the Program, and requesting assistance from the Association in support of the Program during its execution.
14. “Public Expenditure Management Strengthening Program” means a program of actions, supported by technical assistance, designed to

improve policy consistency, efficiency, transparency and accountability in the Recipient's management of public expenditures.

15. "Single Tranche" means the amount of the Financing allocated to the category entitled "Single Tranche" in the table set forth in Part B of Section II of Schedule 1 to this Agreement.

Section II. Modifications to the General Conditions

The modifications to the "International Development Association General Conditions for Credits and Grants", dated July 1, 2005 are as follows:

1. The last sentence of paragraph (a) of Section 2.03 (relating to Applications for Withdrawal) is deleted in its entirety.
2. Sections 2.04 (*Designated Accounts*) and 2.05 (*Eligible Expenditures*) are deleted in their entirety, and the remaining Sections in Article II are renumbered accordingly.
3. Sections 4.01 (*Project Execution Generally*), and 4.09 (*Financial Management; Financial Statements; Audits*) are deleted in their entirety, and the remaining Sections in Article IV are renumbered accordingly.
4. Paragraph (a) of Section 4.05 (renumbered as such pursuant to paragraph 3 above and relating to *Use of Goods, Works and Services*) is deleted in its entirety.
5. Paragraph (c) of Section 4.06 (renumbered as such pursuant to paragraph 3 above) is modified to read as follows:

"Section 4.06. *Plans; Documents; Records*

... (c) The Recipient shall retain all records (contracts, orders, invoices, bills, receipts and other documents) evidencing expenditures under the Financing until two years after the Closing Date. The Recipient shall enable the Association's representatives to examine such records."

6. Section 4.07 (renumbered as such pursuant to paragraph 3 above) is modified to read as follows:

“Section 4.07. *Program Monitoring and Evaluation*”

... (c) The Recipient shall prepare, or cause to be prepared, and furnish to the Association not later than six months after the Closing Date, a report of such scope and in such detail as the Association shall reasonably request, on the execution of the Program, the performance by the Recipient and the Association of their respective obligations under the Legal Agreements and the accomplishment of the purposes of the Financing.”

7. The following terms and definitions set forth in the Appendix are modified or deleted as follows, and the following new terms and definitions are added in alphabetical order to the Appendix as follows, with the terms being renumbered accordingly:

(a) The definition of the term “Eligible Expenditure” is modified to read as follows:

“‘Eligible Expenditure’ means any use to which the Financing is put in support of the Program, other than to finance expenditures excluded pursuant to the Financing Agreement.”

(b) The term “Financial Statements” and its definition as set forth in the Appendix are deleted in their entirety.

(c) The term “Project” is modified to read “Program” and its definition is modified to read as follows:

“‘Program’ means the program referred to in the Financing Agreement in support of which the Financing is made.” All references to “Project” throughout these General Conditions are deemed to be references to “Program”.