

CONFORMED COPY

GRANT NUMBER H337 -NEP

Project Agreement

(Poverty Alleviation Fund Project II)

between

INTERNATIONAL DEVELOPMENT ASSOCIATION

and

POVERTY ALLEVIATION FUND

Dated January 31, 2008

GRANT NUMBER H337-NEP

PROJECT AGREEMENT

AGREEMENT, dated January 31, 2008, entered into between INTERNATIONAL DEVELOPMENT ASSOCIATION (“Association”) and POVERTY ALLEVIATION FUND (“PAF” or “Project Implementing Entity”) (“Project Agreement”) in connection with the Financing Agreement of same date between Nepal (“Recipient) and the Association (the “Financing Agreement”). The Association and the Project Implementing Entity hereby agree as follows:

ARTICLE I – GENERAL CONDITIONS; DEFINITIONS

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

ARTICLE II – PROJECT

- 2.01. The Project Implementing Entity declares its commitment to the objectives of the Project. To this end, the Project Implementing Entity shall carry out the Project in accordance with the provisions of Article IV of the General Conditions, and shall provide promptly as needed, the funds, facilities, services and other resources required for the Project.
- 2.02. Without limitation upon the provisions of Section 2.01 of this Agreement, and except as the Association and the Project Implementing Entity shall otherwise agree, the Project Implementing Entity shall carry out the Project in accordance with the provisions of Schedules 1 through 3 to this Agreement.

ARTICLE III – TERMINATION

- 3.01. For purposes of Section 8.05(c) of the General Conditions, the date on which the provisions of this Agreement shall terminate is twenty (20) years after the date of this Agreement.

ARTICLE IV – REPRESENTATIVE; ADDRESSES

- 4.01. The Project Implementing Entity’s Representative is the Vice-Chairperson of the Board of Directors of PAF.

4.02. The Association's Address is:

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

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

4.03. The Project Implementing Entity's Address is:

Poverty Alleviation Fund
Kathmandu, Nepal

Facsimile:

(977-1) 555-3674

AGREED at Kathmandu, Nepal, as of the day and year first above written.

INTERNATIONAL DEVELOPMENT ASSOCIATION

By /s/Susan G. Goldmark
Authorized Representative

POVERTY ALLEVIATION FUND

By /s/Dr. Ram Prakash Yadav
Authorized Representative

SCHEDULE 1

Execution of the Project

Section I. Subsidiary Financing Agreement; Implementation Arrangements

A. Subsidiary Financing Agreement

1. PAF shall duly perform all its obligations under the Subsidiary Financing Agreement and, except as the Association shall otherwise agree, PAF shall not take or concur in any action which would have the effect of amending, abrogating, assigning or waiving the Subsidiary Financing Agreement or any provision thereof.
2. PAF shall, at the request of the Association, exchange views with the Association with regard to the progress of the Project, the performance of its obligations under this Agreement and under the Subsidiary Financing Agreement, and other matters relating to the purposes of the Financing.
3. PAF shall 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 Financing, or the performance by PAF of its obligations under this Agreement and under the Subsidiary Financing Agreement.

B. Institutional Arrangements

1. PAF shall: (i) ensure that a Board of Directors of PAF is maintained, which shall have general oversight over the Project and meet on a quarterly basis to discuss matters related to the implementation of the Project; and (ii) ensure that the Board of Directors promptly takes all decisions necessary for the effective implementation of the Project and otherwise promptly performs its duties and functions so as not to prevent or interfere with the efficient implementation of the Project.
2. PAF shall, by October 31, 2008, complete the appointment of, and thereafter maintain, an adequate number of key professional staff with skills, qualifications, experience and terms of reference satisfactory to the Association, including without limitation: (i) an Executive Director; (ii) two (2) Accounts Officers; (iii) three (3) Accountants; (iv) one (1) Procurement Specialist; (v) one (1) Environmental Specialist; (vi) one (1) Social Inclusion Specialist; (vii) one (1) Civil Engineer; (viii) one (1) Management Information System (MIS) Assistant; and (ix) one (1) Portfolio Manager in each district in which a Sub-Project is implemented.

3. PAF shall keep the Association promptly informed of changes in membership of the Board of Directors or the Executive Director.

C. Operational Manual and Financial Management Manual

PAF shall:

- (a) carry out its activities under the Project in accordance with the principles, procedures and practices set forth in the Operational Manual and the Financial Management Manual;
- (b) take all measures necessary to ensure that activities of Beneficiaries and POs under the Project are carried out in conformity with the Operational Manual and the Financial Management Manual; and
- (c) not assign, amend, abrogate or waive the Operational Manual or the Financial Management Manual or any provisions thereof if, in the opinion of the Association, such assignment, amendment, abrogation or waiver will materially and adversely affect PAF's, Beneficiaries' or POs' performance or the implementation of the Project or any Sub-Project.

D. Vulnerable Community Development Plan (VCDP); Environmental Management Framework (EMF); Involuntary Resettlement

1. PAF shall implement the VCDP in accordance with the objectives, policies, procedures, time schedules and other provisions set forth therein, to ensure that the activities financed under the Project fully benefit vulnerable people.
2. PAF shall: (i) ensure that all Sub-Projects will be carried out in accordance with the provisions of the EMF and the VCDP; and (ii) not assign, amend, abrogate or waive the EMF and VCDP or any provisions thereof if, in the opinion of the Association, such assignment, amendment, abrogation or waiver will materially and adversely affect the implementation of the Project or any Sub-Project.
3. PAF shall ensure that the carrying out of any Sub-Project does not involve: (a) any involuntary taking of land resulting in: (i) relocation or loss of shelter; (ii) loss of assets or access to assets; or (iii) loss of income sources or means of livelihood, whether or not the affected persons must move to another location; or (b) any involuntary restriction of access to legally designated parks and protected areas resulting in adverse impacts on the livelihood of the affected persons.

E. Anti-Corruption

PAF shall ensure that the Project is carried out in accordance with the provisions of the Anti-Corruption Guidelines.

F. Human Resource Development Plan

PAF shall: (i) by March 31, 2008, submit to the Association a human resource development plan for PAF designed to meet its increased human resource demands under the Project, satisfactory to the Association, including a staff development and training plan; and (ii) thereafter implement such development plan in a manner and with a timetable satisfactory to the Association.

G. Partner Organizations (POs)

1. As part of the implementation of the Project and Sub-Projects, PAF shall contract with POs for the purposes of, *inter alia*, assisting Beneficiaries with the preparation, implementation and supervision of Sub-Projects pursuant to agreements to be entered into between PAF and such POs (PO Agreements) and in accordance with the procedures and on the terms and conditions set forth or referred to in Schedule 2 to this Agreement.
2. PAF shall exercise its rights in relation to financing provided to a PO under a PO Agreement in such manner as to: (i) protect the interests of the Recipient, the Association and PAF; (ii) comply with its obligations under this Agreement and the Subsidiary Financing Agreement; and (iii) achieve the purposes of the Project.

H. Block Grants to Beneficiaries

1. PAF shall provide Block Grants to Beneficiaries under Parts A, B and C of the Project pursuant to agreements to be entered into between PAF and such Beneficiaries (Sub-Project Grant Agreements) and in accordance with the procedures and on the terms and conditions set forth or referred to in Schedule 2 to this Agreement.
2. PAF shall exercise its rights in relation to each Block Grant provided to a Beneficiary under a Sub-Project Grant Agreement in such manner as to: (i) protect the interests of the Recipient, the Association and PAF; (ii) comply with its obligations under this Agreement and the Subsidiary Financing Agreement; and (iii) achieve the purposes of the Project.
3. Except as the Association shall otherwise agree, PAF shall ensure that:
 - (a) for purposes of financing Sub-Projects under Part A of the Project, no single Beneficiary shall receive out of the proceeds of the Financing an amount, which either by itself or together with any other outstanding amount so received by such Beneficiary will exceed the equivalent of twenty percent (20%) of the amount from time to time allocated to

Category 1 set forth in the table in Part A of Section IV of Schedule 2 to the Financing Agreement; and

- (b) for purposes of financing Sub-Projects under Part B of the Project, no single Beneficiary shall receive out of the proceeds of the Financing an amount, which either by itself or together with any other outstanding amount so received by such Beneficiary will exceed the equivalent of twenty-five percent (25%) of the amount from time to time allocated to Category 1 set forth in the table in Part A of Section IV of Schedule 2 to the Financing Agreement; and
- (c) for purposes of financing Sub-Projects under Part C of the Project, no single Beneficiary shall receive out of the proceeds of the Financing an amount, which either by itself or together with any other outstanding amount so received by such Beneficiary will exceed the equivalent of one hundred thousand Dollars (US\$100,000) of the amount from time to time allocated to Category 1 set forth in the table in Part A of Section IV of Schedule 2 to the Financing Agreement.

Section II. Project Monitoring, Reporting and Evaluation

A. Project Reports

- 1. The Project Implementing Entity shall monitor and evaluate the progress of the Project and prepare Project Reports in accordance with the provisions of Section 4.08 of the General Conditions and on the basis of the indicators set forth in Schedule 3 to this Agreement. Each Project Report shall cover the period of a Fiscal Year trimester, and shall be furnished to the Association not later than forty-five (45) days after the end of the period covered by such report.
- 2. The Project Implementing Entity shall prepare and furnish to the Association not later than six (6) months after the Closing Date the report and the plan referred to in Section 4.08(c) of the General Conditions.

B. Financial Management, Financial Reports and Audits

- 1. The Project Implementing Entity shall maintain a financial management system and prepare financial statements in accordance with consistently applied accounting standards acceptable to the Association, both in a manner adequate to reflect the operations and financial condition of the Project Implementing Entity, including the operations, resources and expenditures related to the Project.

2. Without limitation on the provisions of Part A of this Section, the Project Implementing Entity shall prepare and furnish to the Association as part of the Project Report not later than forty-five (45) days after the end of each Fiscal Year trimester, interim un-audited financial reports for the Project covering the Fiscal Year trimester, in form and substance satisfactory to the Association.
3. The Project Implementing Entity shall have its financial statements referred to above audited by independent auditors acceptable to the Association, in accordance with consistently applied auditing standards acceptable to the Association. Each audit of these financial statements shall cover the period of one Fiscal Year of the Project Implementing Entity. The audited financial statements for each such period shall be furnished to the Association not later than six (6) months after the end of such period.

Section III. Procurement

All goods, works and services required for the Project and to be financed out of the proceeds of the Financing shall be procured in accordance with the provisions of Section III of Schedule 2 to the Financing Agreement.

SCHEDULE 2

Terms and Conditions of, and Procedures for Contracting with POs and Provision of Block Grants to Beneficiaries

Part A: Contracting with POs

Except as the Association shall otherwise agree, POs shall be contracted by PAF for the purposes of *inter alia*, assisting Beneficiaries with the preparation, implementation and supervision of Sub-Projects.

Terms and Conditions; Procedures

- (a) PAF shall, through an advertisement to be published in national newspapers from time to time, invite POs to submit written proposals on how they would facilitate Beneficiaries mobilization and Sub-Projects preparation and implementation.
- (b) On the basis of such proposals, PAF shall carry out a series of preliminary appraisals, desk appraisals and field appraisals of the proposed POs in accordance with the Operational Manual, in order to establish, *inter alia*, whether the proposed POs can:
 - (i) satisfy the relevant eligibility criteria;
 - (ii) accept PAF's operational guidelines;
 - (iii) demonstrate compatibility with PAF's strategies; and
 - (iv) demonstrate that they employ, or can employ, the operational policies, procedures and human resources required in furtherance of the proposed partnership between themselves and PAF.
- (c) Without limiting the generality of sub-paragraphs (a) and (b) of this Part A, in order to receive financing from PAF for its services, each eligible PO shall enter into a written agreement with PAF (PO Agreement) pursuant to which PAF shall obtain rights adequate to protect the interests of the Recipient, the Association and PAF, including the right to:
 - (i) require that the PO's activities under the Project be carried out:
 - (aa) with due diligence and efficiency;

- (bb) in accordance with sound technical, economic, financial, managerial, environmental and social standards; and
 - (cc) in accordance with the provisions of the Operational Manual, the Financial Management Manual, the EMF, the VCDP and the Anti-Corruption Guidelines applicable to recipients of grant proceeds other than the Recipient;
- (ii) require that:
- (aa) adequate records and accounts to reflect the operations, resources and expenditures related to the PO's activities under the Project be maintained; and
 - (bb) at the Recipient's or the Association's or PAF's request, such records and accounts be audited by independent auditors acceptable to the Association, in accordance with consistently applied auditing standards acceptable to the Association, and, as so audited, promptly furnished to the Recipient, the Association and PAF;
- (iii) inspect by itself, or jointly with the Association, if the Association shall so request, the operations of the PO and any relevant records and documents;
- (iv) obtain all such information as the Association shall reasonably request, regarding the administration, operation and financial condition of the PO and its activities for which the financing from PAF is made;
- (v) suspend or terminate the right of the PO to use the proceeds of the financing from PAF, or obtain a refund of all or any part of the amount of such financing then withdrawn, upon the PO's failure to perform any of its obligations under the PO Agreement.

Part B: Provision of Block Grants to Beneficiaries

1. Eligibility Criteria

- (a) Except as the Association shall otherwise agree, Block Grants shall be made only to Beneficiaries who satisfy the eligibility criteria set forth in the Operational Manual, which shall include that:

- (i) the Beneficiaries shall be considered poor or vulnerable under the definition adopted by PAF; and
 - (ii) the Beneficiaries shall conduct their affairs in a participatory manner including women and disadvantaged groups.
- (b) Eligibility criteria for SSIPs set forth in the Operational Manual shall include the following:
- (i) the SSIPs shall benefit the Beneficiary community population and shall be technically sound, simple and manageable by the community; and
 - (ii) the SSIPs shall not be on PAF's negative list set forth in the Operational Manual.
- (c) Eligibility criteria for IGSPs set forth in the Operational Manual shall include the following:
- (i) the IGSPs shall be able to generate income; and
 - (ii) the IGSPs shall not be on PAF's negative list set forth in the Operational Manual.

2. Terms and Conditions

Except as the Association shall otherwise agree, Block Grants shall be made: (i) on a non-reimbursable basis; and (ii) denominated in Nepalese Rupee.

3. Procedures

- (a) Proposals for Sub-Projects may be initiated or sponsored by Beneficiaries in their own capacity or liaising with POs, as the case may be, shall identify the type of Sub-Project and the Beneficiary, describe the works or goods to be financed and any goods or works to be provided in-kind by the Beneficiary, and identify the PO, if any, and its facilitating role.
- (b) For each Block Grant, PAF shall enter into a written agreement with the concerned Beneficiary (Sub-Project Grant Agreement) pursuant to which PAF shall obtain rights adequate to protect the interests of the Recipient, the Association and PAF, including the right to:
 - (i) require that the Sub-Project for which the Block Grant is made be carried out:

- (aa) with due diligence and efficiency;
 - (bb) in accordance with sound technical, economic, financial, managerial, environmental and social standards; and
 - (cc) in accordance with the provisions of the Operational Manual, the Financial Management Manual, the EMF, the VCDP and the Anti-Corruption Guidelines applicable to recipients of grant proceeds other than the Recipient;
- (ii) require that:
- (aa) adequate records and accounts to reflect the operations, resources and expenditures related to the Sub-Project be maintained; and
 - (bb) at the Recipient's or the Association's or PAF's request, such records and accounts be audited by independent auditors acceptable to the Association, in accordance with consistently applied auditing standards acceptable to the Association, and, as so audited, promptly furnished to the Recipient, the Association and PAF;
- (iii) require that:
- (aa) the goods, works and services to be financed out of the proceeds of the Block Grant be procured in accordance with the provisions of Schedule 2 to the Financing Agreement; and
 - (bb) such goods, works and services be used exclusively in the carrying out of the Sub-Project for which the Block Grant is made;
- (iv) inspect by itself, or jointly with the Association, if the Association shall so request, the goods, works, sites, plants and construction included in the Sub-Project for which the Block Grant is made, the operations thereof and any relevant records and documents;
- (v) obtain all such information as the Association shall reasonably request, regarding the administration, operation and financial condition of the Sub-Project for which the Block Grant is made;

- (vi) suspend or terminate the right of the Beneficiary to use the proceeds of the Block Grant, or obtain a refund of all or any part of the amount of the Block Grant then withdrawn, upon the Beneficiary's failure to perform any of its obligations under the Sub-Project Grant Agreement; and
- (vii) require that:
 - (aa) the Beneficiary identify and approve the Sub-Project for which the Block Grant is made through an open and participatory process;
 - (bb) the Beneficiary sign the Sub-Project Grant Agreement in which its responsibilities are clearly defined;
 - (cc) the Beneficiary contribute towards the capital cost of the Sub-Project for which the Block Grant is made, such contribution varying according to the capacity to pay, as set forth in the Operational Manual;
 - (dd) the Beneficiary implement the Sub-Project for which the Block Grant is made within a stipulated time and budget;
 - (ee) the Beneficiary open two separate bank accounts (a non-operating account and an operating account), to be operated by at least two signatories, and maintain records of all receipts and payments relating to the Sub-Project for which the Block Grant is made;
 - (ff) the Beneficiary submit its work to supervision and certification for quality and adherence to specifications by PAF, having the right to suspend payments under the Block Grant in respect of sub-standard work until such time as such work has been rectified;
 - (gg) the Beneficiary be fully responsible for the operation and maintenance of the Sub-Project for which the Block Grant is made; and
 - (hh) the Beneficiary make cash or in kind contributions for the implementation of the Sub-Project for which the Block Grant is made.

SCHEDULE 3

Performance Indicators for the Project

INDICATOR	MIDTERM (On or about June 30, 2010)	FINAL (On or about September 30, 2012)
1. Number of Sub-Projects.	2500	6000
2. Number of groups of Beneficiaries.	3500	7000
3. Percentage of women membership in groups.	25%	40%
4. Percentage of <i>Dalit</i> membership in groups.	10%	20%
5. Percentage of indigenous membership in groups.	10%	20%
6. Percentage of Madhesi membership in groups.	10%	20%
7. Number of VDCs covered.	600	1200
8. Amount of contribution of communities.	US\$2,000,000	US\$7,000,000
9. Number of Beneficiaries trained.	1500	3000