

CONFORMED COPY

CREDIT NUMBER 3673 CE

Development Credit Agreement

(Renewable Energy for Rural Economic Development Project)

between

DEMOCRATIC SOCIALIST REPUBLIC OF SRI LANKA

and

INTERNATIONAL DEVELOPMENT ASSOCIATION

Dated July 12, 2002

CREDIT NUMBER 3673 CE

DEVELOPMENT CREDIT AGREEMENT

AGREEMENT, dated July 12, 2002, between DEMOCRATIC SOCIALIST REPUBLIC OF SRI LANKA (the Borrower) and INTERNATIONAL DEVELOPMENT ASSOCIATION (the Association).

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

Association to assist in the financing of the Project;

(B) by the Global Environment Facility Trust Fund Grant Agreement (the Grant Agreement) of even date herewith between the Borrower (in such capacity, the Recipient) and the International Bank for Reconstruction and Development (the Bank), acting as an implementing agency of the Global Environmental Facility, the Bank has agreed to make a grant (the GEF Trust Fund Grant) to the Recipient in an amount equal to six million four hundred thousand Special Drawing Rights (SDR 6,400,000) to assist in financing the Project on the terms and conditions set forth in the Grant Agreement; and

(C) the Project shall be carried out by DFCC Bank with the Borrower's assistance, and as part of such assistance, the Borrower shall make available to DFCC Bank part of the proceeds of the credit to be provided under Article II of this Agreement (the Credit) and part of the proceeds of the GEF Trust Fund Grant to be provided under Article II of the Grant 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 IDA Project Agreement of even date herewith between the Association and DFCC Bank;

NOW, THEREFORE, the parties hereto, hereby, agree as follows:

ARTICLE I

General Conditions; Definitions

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

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) "Administration Agreement" means the agreement between the Borrower and DFCC Bank for implementing the Project, including all schedules, supplemental agreements and amendments made from time to time, approved by the Association;

(b) "Administrative Unit" means the Administrative Unit established by DFCC Bank, which is responsible for implementing the Project, in accordance with the terms and conditions of the Administration Agreement;

(c) "DFCC Bank" means DFCC Bank, a body corporate established under the Development Finance Corporation of Ceylon Act No. 35 of 1955, as amended, and any successor entity to DFCC Bank recognized by the Borrower in accordance with the terms of the Administration Agreement;

(d) "Eligibility Criteria" means the Borrower's list of criteria, acceptable to the Association, to determine whether an entity qualifies to be a Participating Credit Institution for the purposes of this Project;

(e) “Eligible Categories” means categories (1), (2) (a), (2) (b), (3), (4) (a), (4) (b), (4) (c) and (5) set forth in the table in Part A.1 of Schedule 1 to this Agreement;

(f) “Eligible Expenditures” means the expenditures for goods, works and services referred to in Section 2.02 of this Agreement;

(g) “Environment and Social Assessment Framework” means Borrower’s framework document dated February 20, 2002, and any amendments to such document, satisfactory to the Association, that shall: (i) enable the Borrower to assess, among other things, the Project’s environmental and social impacts; and (ii) where applicable, govern the preparation of environmental management plans, resettlement and rehabilitation plans, indigenous peoples development plans and other appropriate mechanisms, satisfactory to the Association, required to mitigate and monitor any adverse impacts from carrying out the Project;

(h) “Fiscal Year” means the Fiscal Year of the Borrower beginning on January 1 of a calendar year and ending on December 31 of the calendar year;

(i) “Free Limit Sub-loan” means any Sub-loan (as such term is hereinafter defined) for an Investment Project in an amount not exceeding \$1,000,000;

(j) “GEF Project Agreement” means the agreement between the Bank and DFCC Bank, of even date herewith relating to carrying out the Project, including any amendments made, from time to time, and all schedules and supplemental agreements thereto;

(k) “Grant Agreement” means the agreement of even date herewith between the Recipient and the Bank, acting as an implementing agency of the Global Environmental Facility, relating to the Project, as the same may be amended from time to time, and such term includes all schedules and agreements supplemental to the Grant Agreement;

(l) “IDA Project Agreement” means the agreement between the Association and DFCC Bank of even date herewith relating to carrying out the Project, including any amendments made, from time to time, and all schedules and supplemental agreements thereto;

(m) “IDA Special Account” means the account referred to in Part B.1 of Schedule 1 to this Agreement;

(n) “Investment Enterprise” means an entity or household that intends to carry out an Investment Project for which the entity or household receives or is expected to receive: (i) a Sub-loan from a Participating Credit Institution (as such terms are hereinafter defined); or (ii) a Sub-grant or an Investment Project Preparation Grant from the Borrower (as such terms are hereinafter defined), out of the proceeds of the Credit;

(o) “Investment Project” means any of the following renewable energy or energy conservation projects that qualify under the Operating Guidelines (as hereinafter defined) for a Sub-loan, Sub-grant or an Investment Project Preparation Grant under the Project:

(i) grid-connected hydro, wind and biomass energy projects;

(ii) solar photo voltaic projects;

(iii) community-based wind, hydro and biomass energy projects;

(iv) energy efficiency, conservation and demand-side management projects;

and

(v) other eligible renewable energy projects that satisfy the Operating Guidelines;

(p) “Investment Project Preparation Grant” means a grant made by the Borrower, utilizing the proceeds of the GEF Trust Fund Grant and the Credit, to assist an Investment Enterprise in preparing an Investment Project;

(q) “Operating Guidelines” means the Borrower’s operating guidelines dated May 10, 2002, for implementing the Project, satisfactory and acceptable to the Association, including any amendments made to these guidelines with the Association’s agreement;

(r) “Participation Agreement” means a participation agreement, in form and substance acceptable to the Association, to be entered between the Borrower and a Participating Credit Institution, relating among other things, to Sub-loans under Part A of the Project;

(s) “Participating Credit Institution” means any financial institution established and operating in accordance with the laws of the Borrower, that satisfies the Eligibility Criteria to participate in the Project and executes a Participation Agreement for this purpose;

(t) “Project Implementation Plan” means Borrower’s Project Implementation Plan dated May 10, 2002, approved by the Association, containing, among other things, financial projections or forecasts for the Project, details regarding procurement, format and content of project financial reports, monitoring and performance indicators and procedures to be used for implementation of the Project, and shall include any accompanying schedules or exhibits and any amendments or updates made, from time to time, by the Borrower or DFCC Bank with the Association’s agreement;

(u) “Project Management Report” means each report prepared in accordance with Section 4.02 of this Agreement;

(v) “Rs” and “rupees” means the currency of the Borrower;

(w) “Sub-grant” means a grant to an Investment Enterprise by the Borrower, out of the proceeds of the Credit or the GEF Trust Fund Grant, for an Investment Project in accordance with the Operating Guidelines; and

(x) “Sub-loan” means a loan or lease financing made, or proposed to be made, to an Investment Enterprise by a Participating Credit Institution, out of the Credit proceeds, for an Investment Project under Part A of the Project, in accordance with the Operating Guidelines, and the Participation Agreement between the Participating Credit Institution and the Borrower, and, unless the context otherwise requires, the term “Sub-loan” includes a Free-Limit Sub-loan.

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 fifty-nine million three hundred thousand Special Drawing Rights (SDR 59,300,000).

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 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.

Section 2.03. The Closing Date shall be June 30, 2008, or such later date as the Association shall establish. The Association shall promptly notify the Borrower of such later date.

Section 2.04. (a) The Borrower shall pay to the Association a commitment charge on the principal amount of the Credit not withdrawn from time to time at a rate to be set by the Association as of June 30 of each year, but not to exceed the rate of one-half of one percent (1/2 of 1%) per annum.

(b) The commitment charge shall accrue: (i) from the date sixty days after the date of this Agreement (the accrual date) to the respective dates on which amounts shall be withdrawn by the Borrower from the Credit Account or canceled; and (ii) at the rate set as of the June 30 immediately preceding the accrual date and at such other rates as may be set from time to time thereafter pursuant to paragraph (a) above. The rate set as of June 30 in each year shall be applied from the next date in that year specified in Section 2.06 of this Agreement.

(c) The commitment charge shall be paid: (i) at such places as the Association shall reasonably request; (ii) without restrictions of any kind imposed by, or in the territory of, the Borrower; and (iii) in the currency specified in this Agreement for the purposes of Section 4.02 of the General Conditions or in such other eligible currency or currencies as may from time to time be designated or selected pursuant to the provisions of that Section.

Section 2.05. The Borrower shall pay to the Association a service charge at the rate of three-fourths of one percent (3/4 of 1%) per annum on the principal amount of the Credit withdrawn and outstanding from time to time.

Section 2.06. Commitment charges and service charges shall be payable semiannually on June 15 and December 15 in each year.

Section 2.07. (a) Subject to paragraphs (b), (c) and (d) below, the Borrower shall repay the principal amount of the Credit in semiannual installments payable on each June 15 and December 15 commencing December 15, 2012 and ending June 15, 2042. Each installment to and including the installment payable on June 15, 2012 shall be one percent (1%) of such principal amount, and each installment thereafter shall be two percent (2%) of such principal amount.

(b) Whenever: (i) the Borrower's per capita gross national product (GNP), as determined by the Association, shall have exceeded for three consecutive years the level established annually by the Association for determining eligibility to access the Association's resources; and (ii) the Bank shall consider the Borrower creditworthy for Bank lending, the Association may, subsequent to the review and approval thereof by the Executive Directors of the Association and after due consideration by them of the development of the Borrower's economy, modify the repayment of installments under paragraph (a) above by:

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

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

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

Section 2.08. 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 this Agreement, shall cause DFCC Bank to perform, in accordance with the provisions of this agreement, the IDA Project Agreement, the GEF Project Agreement and the Administration Agreement, all the obligations of DFCC Bank and the Administrative Unit 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 DFCC Bank to perform such obligations, and shall not take or permit to be taken any action which would prevent or interfere with such performance.

(b) The Borrower shall make available to the Administrative Unit on a grant basis

the proceeds of the Credit allocated, from time to time, for: (i) Sub-grants to be made to Investment Enterprises under Part A of the Project (finance for Investment Projects); and (ii) Investment Project Preparation Grants and other expenditure for activities under Part B (technical assistance) and Part C of the Project (project implementation assistance) in accordance with the Administration Agreement to be entered into between the Borrower and DFCC Bank.

(c) The Borrower shall relend proceeds of the Credit allocated from time to time for Sub-loans to be made under Part A of the Project (finance for Investment Enterprises) to Participating Credit Institutions in accordance with Participation Agreements to be entered into between the Borrower and each Participating Credit Institution.

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

(e) Without limitation upon the provisions of paragraph (a) of this Section and except as the Borrower and the Association shall otherwise agree:

(i) the Borrower shall ensure that the Project is carried out in accordance with its obligations set forth in Schedule 3 (Borrower's Project Obligations) and Schedule 4 (Investment Projects) to this Agreement; and

(ii) the Borrower shall cause DFCC Bank to carry out the Project in accordance with the Implementation Program set forth in Schedule 2 to the IDA Project Agreement.

Section 3.02. (a) For each Fiscal Year, beginning with Fiscal Year 2003 until completion of the Project, the Borrower shall: (i) take appropriate and necessary action in accordance with its budgetary procedures to ensure that sufficient allocations are made for Project expenditures, which are not otherwise financed by the Credit or the GEF Trust Fund Grant proceeds; and (ii) take necessary measures to ensure that the funds allocated in accordance with clause (i) of this sub-section 3.02 (a) are made available, in a timely manner, to the Administrative Unit.

(b) For each Fiscal Year, beginning with Fiscal Year 2003, until completion of the Project, the Borrower shall: (i) take appropriate and necessary action in accordance with its budgetary procedures to ensure that sufficient allocations are made for Project expenditures, to be incurred out of the proceeds of the Credit and the GEF Trust Fund Grant; and (ii) take necessary measures to ensure that the funds allocated in accordance with clause (i) of this sub-section 3.02 (b) are made available, in a timely manner, to the Administrative Unit.

Section 3.03. Except as the Association shall otherwise agree, procurement of the goods, works and consultants' services required for the Project and to be financed out of the proceeds of the Credit shall be governed by the provisions of Schedule 1 to the IDA Project Agreement.

Section 3.04. For the purposes of Section 9.06 of the General Conditions and without limitation thereto, the Borrower shall:

(a) 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 Borrower and the Association, a plan designed to ensure the sustainability of the Project; and

(b) afford the Association a reasonable opportunity to exchange views with the Borrower on said plan.

Section 3.05. 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 the Project shall be carried out by DFCC Bank pursuant to Section 2.03 of the IDA 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 Project Management Reports, the Borrower shall, or shall cause DFCC Bank to:

- (i) maintain, in accordance with sound accounting practices, records and separate accounts reflecting such expenditures;
- (ii) ensure that all records (contracts, orders, invoices, bills, receipts and other documents) evidencing such expenditures are retained until at least one year after the Association has received the audit report for the Fiscal Year in which the last withdrawal from the Credit Account was made; and
- (iii) enable the Association's representatives to examine such records.

(b) The Borrower shall, or shall cause DFCC Bank to:

- (i) have the records and accounts referred to in paragraph (a) (i) of this Section and those for the IDA Special Account for each Fiscal Year audited, in accordance with appropriate auditing principles consistently applied, by independent auditors acceptable to the Association;
- (ii) furnish to the Association as soon as available, but in any case not later than six months after the end of each such Fiscal 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 Project Management Reports 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.

Section 4.02. The Borrower shall prepare, or shall cause the Administrative Unit to prepare, in accordance with guidelines acceptable to the Association, and furnish to the Association not later than 45 days after the end of each calendar quarter, a Project Management Report for such period, which:

- (a) (i) 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

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

ARTICLE V

Remedies of the Association

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

- (a) DFCC Bank or the Administrative Unit shall have failed to perform any of its obligations under this Agreement, the Grant Agreement, the IDA Project Agreement, the GEF Project Agreement, or the Administration Agreement;
- (b) as a result of events which have occurred after the date of this Agreement, an extraordinary situation shall have arisen which shall make it improbable that DFCC Bank or the Administrative Unit will be able to perform its obligations under this Agreement, the Grant Agreement, the IDA Project Agreement, the GEF Project Agreement, or the Administration Agreement;
- (c) the legal framework or the principal corporate and organizational documents governing DFCC Bank shall have been amended, suspended, abrogated, repealed or waived so as to affect materially and adversely the ability of DFCC Bank to perform any of its obligations under this Agreement, the Grant Agreement, the IDA Project Agreement, the GEF Project Agreement, or the Administration Agreement;
- (d) the Borrower or any appropriate legal or regulatory authority within its jurisdiction shall have taken any action for the dissolution or disestablishment of DFCC Bank or for the suspension of its operations;
- (e) the Recipient shall have failed to perform any of its obligations under the Grant Agreement; and
- (f) the Recipient's right to withdraw the proceeds of the GEF Trust Fund Grant shall have been suspended, cancelled or terminated, in whole or in part, by the Bank pursuant to the terms of the Grant Agreement.

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

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

(b) any of the events specified in paragraphs (e) and (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 the Development Credit Agreement within the meaning of Section 12.01 (b) of the General Conditions:

(a) all conditions precedent to the effectiveness of the Grant Agreement and the GEF Project Agreement have been fulfilled other than those related to the effectiveness of this Agreement;

(b) the Administration Agreement has been entered into by the Borrower and DFCC Bank;

(c) Participation Agreements have been entered into by the Borrower with at least two Participating Credit Institutions;

(d) the Borrower has taken appropriate and necessary action in accordance with its budgetary procedures to ensure that sufficient allocations are made for Project expenditures for the Fiscal Year 2002, which are not otherwise financed by the Credit or the GEF Trust Fund Grant proceeds;

(e) in accordance with the allocations made under sub-paragraph (d), above, the Borrower has made available to DFCC Bank necessary funds for Project expenditures in Fiscal Year 2002 for the quarterly period following the Effective Date, which are not otherwise financed by the Credit and the GEF Trust Fund Grant proceeds; and

(f) the Borrower has taken appropriate and necessary action in accordance with its budgetary procedures to ensure that sufficient allocations are made for Project expenditures to be incurred in Fiscal Year 2002 out of the proceeds of the Credit and the GEF Trust Fund Grant.

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

(a) the IDA Project Agreement has been duly authorized or ratified by DFCC Bank, and is legally binding upon DFCC Bank in accordance with their respective terms; and

(b) the Administration Agreement has been duly authorized or ratified by, and executed and delivered on behalf of, the Borrower and DFCC Bank and is legally binding upon the Borrower and DFCC Bank 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 provisions of Section 5.02 of this Agreement shall cease and determine on the date on which this Agreement shall terminate or on the date twenty years following the date of this agreement, whichever shall be earlier.

ARTICLE VII

Representative of the Borrower; Addresses

Section 7.01. The Secretary, Ministry of Finance, or the Director General, External Resources Department, Ministry of Finance, of the Borrower is designated as 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 Finance
The Secretariat
Colombo 1, Sri Lanka

Cable address:	Telex:	Facsimile:
SECMINFIN	FINMIN 21409	94-1-449823
	FORAID 21232	94-1-447633

For the Association:

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)	202-477-6391

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

DEMOCRATIC SOCIALIST REPUBLIC OF SRI LANKA

By /s/ Charitha Ratwatte

Authorized Representative

INTERNATIONAL DEVELOPMENT ASSOCIATION

By /s/ Peter Harrold

Country Director, Sri Lanka

SCHEDULE 1

Withdrawal of the Proceeds of the Credit

Part 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:

<u>Category</u>	<u>Amount of the Credit Allocated (Expressed in SDR Equivalent)</u>	<u>% of Expenditures to be Financed</u>
(1) Sub-loans under Part A of the Project (finance for Investment Projects)	52,000,000	80% of amounts disbursed in respect of Sub-loans
(2) Investment Project: Preparation Grants		
(a) Grants made for preparation activities and feasibility studies carried out by tax-exempt consultants and non-governmental entities	380,000	100% of amounts disbursed for preparation activities and feasibility studies
(b) Other grants for	500,000	80% of amounts

	preparation activities and studies		disbursed for preparation activities and feasibility studies
(3)	Sub-grants under Part A of the Project	1,000,000	100% of amounts disbursed in respect of Sub-grants
(4)	Consultants' services, training and internal audit expenses		
(a)	Individual consultants	100,000	80%
(b)	Consulting firms	400,000	80%
(c)	Training, workshops and study tours	100,000	80%
(5)	Goods	80,000	100% of foreign expenditures; 100% of the ex-factory cost of local expenditures; 75% of local expenditures
(6)	Unallocated	4,740,000	
	TOTAL	59,300,000	

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; and

(c) the term "tax-exempt consultants and non-governmental entities" means those consultants and non-governmental entities who are not liable to tax under the laws of the Borrower.

3. Notwithstanding the provisions of paragraph 1 above: no withdrawals shall be made in respect of payments for a Sub-loan under Category (1), which is not a Free-Limit Sub-loan, without the approval of the Association.

Part B: IDA Special Account

1. The Borrower shall open and maintain in the Central Bank of Sri Lanka a special deposit account on terms and conditions satisfactory to the Association. 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 IDA Special Account in accordance with the provisions of this Schedule. Payments out of the IDA Special Account shall be made exclusively for Eligible Expenditures. For each payment made by the Borrower out of the IDA 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.

2. Except as the Association shall otherwise agree, after the Association has received evidence satisfactory to it that the IDA Special Account has been duly opened, withdrawals from the Credit Account of amounts to be deposited into the IDA Special Account shall be made as follows:

(a) Each application for withdrawal from the Credit Account shall be supported by a Project Management Report.

(b) 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 IDA Special Account an amount equal to the lesser of: (i) the amount so requested; and (ii) 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 report to be remaining in the IDA Special Account, shall not exceed the equivalent of \$15,000,000. Each such deposit into the IDA Special Account shall be withdrawn by the Association from the Credit Account under one or more of the IDA Special Account's Eligible Categories.

3. Notwithstanding the provisions of Part B.2 of this Schedule, the Association shall not be required to make further deposits into the IDA 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 4.02 of this Agreement;

(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 4.01(b)(ii) of this Agreement, 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 the IDA Special Account; or (B) the records and accounts reflecting expenditures with respect to which withdrawals were made on the basis of Project Management Reports.

4. The Association shall not be required to make further deposits into the IDA 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 IDA Special Account may be made and what procedures should be followed for making such deposits, and shall notify the Borrower of its determination.

5. (a) If the Association determines at any time that any payment out of the IDA 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 the IDA Special Account (or, if the Association shall so request, refund to the Association) an amount equal to the amount of such payment.

(b) If the Association determines at any time that any amount outstanding in the IDA 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 IDA Special Account.

(d) Refunds to the Association made pursuant to sub-paragraph (a), (b) or (c) of this paragraph 5 shall be credited to the Credit Account for subsequent withdrawal or for cancellation in accordance with the provisions of the Development Credit Agreement.

SCHEDULE 2

Description of the Project

The objectives of the Project are to support Sri Lanka in: (i) improving rural quality of life and prospects for income generation by providing off-grid electricity to remote rural communities; and (ii) promoting private sector power generation for the grid from renewable energy resources. The Project will support private sector and community-based development models, and help develop initiatives for productive use of electricity to increase rural household incomes and improve the delivery of rural social services, such as health and education.

The Project consists of the following Parts, subject to any modifications that the Borrower and the Association may agree upon from time to time to achieve the objectives of the Project:

Part A: **Finance for Investment Projects**

Financial assistance for Investment Enterprises to carry out Investment Projects through Sub-loans and Sub-grants.

Part B: **Technical Assistance**

Support for renewable energy, energy use and energy conservation projects on a cost-sharing or full-cost basis through the provision of advisory services including:

1. Promoting and providing development support, including Investment Project Preparation Grants, for Investment Projects.
2. Providing support for policy development, modern technology introductions, market promotion, sustainability, and capacity building for renewable energy, energy efficiency, conservation and demand-side management.
3. Promoting cross-sectoral energy applications for rural income generation and social development.
4. Monitoring and evaluation to assess Project impacts.

Part C: Project Implementation Assistance

Support for the Administrative Unit in the following areas:

1. Project administration, promotion and coordination.
2. Developing plans for Project sustainability and continued expansion of the renewable energy industry.
3. Carrying out monitoring and evaluation exercises, including surveys and audits, for the Project.

* * *

The Project is expected to be completed by December 31, 2007.

SCHEDULE 3

Borrower's Project Obligations

1. The Borrower shall develop standards for the recycling and disposal of batteries used in solar home systems within two years of the Effective Date of this Agreement.
2. The Borrower shall, or shall cause DFCC Bank to:
 - (a) maintain policies and procedures adequate to enable it to monitor and evaluate on an ongoing basis, in accordance with indicators acceptable to the Association, the carrying out 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 by December 31, 2004, 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 the Project during the period preceding the date of said report and setting out the measures recommended to ensure the efficient carrying out 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, 2005, or such later date as the Association shall agree, the report referred to in paragraph (b) of this Section, and, thereafter,

take all measures required to ensure the efficient completion 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.

SCHEDULE 4

Investment Projects

Participating Credit Institutions and Eligibility Criteria

1. (a) The Borrower, or an entity authorized by the Borrower, shall enter into Participation Agreements with Participating Credit Institutions, satisfactory to the Association, that shall contain the terms and conditions for making Sub-loans.

(b) Each Participating Credit Institution that enters into a Participation Agreement with the Borrower or an entity authorized by the Borrower shall satisfy the applicable Eligibility Criteria.

(c) By no later than September 30 of each year following the Effective Date, the Borrower shall: (i) carry out an independent assessment of each of the Participating Credit Institutions under the Project, including their compliance with the Eligibility Criteria, and (ii) transmit the results of such review to the Association within thirty days following the date of each such review.

(d) If, at any time, a Participating Credit Institution fails to satisfy the Eligibility Criteria, the Borrower or an entity authorized by the Borrower shall take such action as may be appropriate and necessary in consultation with the Association including:

(i) suspending or terminating the right of the Participating Credit Institution to use the proceeds of the Credit; or

(ii) declaring the principal amount of that Participating Credit Institution's share of the proceeds of the Credit then outstanding to be due and payable immediately together with the service charges thereon.

Appraising Investment Projects

2. Except as the Association may otherwise agree, the Borrower shall ensure, or shall cause the Administrative Unit or the Participating Credit Institutions (as the case may be) to ensure, that Investment Projects shall be promoted, identified, appraised, approved, carried out and monitored in accordance with the procedures and other provisions set forth or referred to in this Agreement, the Participation Agreement, the Operating Guidelines and, if applicable, the Eligibility Criteria.

Environmental and Social Assessment Framework

3. (a) The Borrower shall ensure that Investment Projects, which receive Sub-grants under the Project, comply with the environmental, resettlement and social standards set forth in the Environment and Social Assessment Framework.

(b) The Borrower shall cause each Participating Credit Institution to ensure that Investment Projects, which receive Sub-loans under the Project, comply with the environmental, resettlement and social standards set forth in the Environment and Social Assessment Framework.

4. In accordance with paragraph 3, above, the Borrower shall ensure, or shall cause each Participating Credit Institution to ensure, that:

(a) each Investment Enterprise applying for financing under the Project provides evidence satisfactory to the Association and the Borrower or the Participating Credit Institution (as the case may be), showing that the Investment Project in respect of which the application has been made has been prepared in accordance with the standards referred in paragraph 3, above.

(b) An application for financing an Investment Project shall include, where applicable, among other things, an environmental assessment, an environmental management plan, a resettlement and rehabilitation plan and an indigenous peoples development plan, for such Investment Project, each of which shall be satisfactory and acceptable to the Association.

(c) The Borrower shall engage, or shall cause the Administrative Unit to engage, by no later than December 31, 2002, a consultant, with qualifications and experience satisfactory to the Association, to review, for the purposes of sub-paragraphs (a) and (b), above, applications for financing Investment Projects from proceeds of the Credit.

Investment Project Documentation

5. Under the terms of each Participation Agreement, the Borrower shall cause each Participating Credit Institution to ensure that appropriate and sufficient legal and financing documentation is made available by an Investment Enterprise to a Participating Credit Institution prior making a Sub-loan to the Investment Enterprise.

6. In accordance with the terms of the Operating Guidelines and the Participation Agreement, the Borrower shall, or shall cause the Administrative Unit, to audit or monitor compliance by each Participating Credit Institution with the provisions of the applicable Participation Agreement, which relate to paragraph 5, above.

7. The Borrower shall ensure, or shall cause the Administrative Unit to ensure, that appropriate and sufficient legal and financing documentation is made available by an Investment Enterprise prior to making a Sub-grant or an Investment Project Preparation Grant to the Investment Enterprise.

8. In accordance with the terms of the Operating Guidelines, the documentation referred to in paragraphs 5 and 7, above, shall contain necessary and appropriate provisions to protect the interests of the Association, the Borrower, and, where applicable, the Administrative Unit and the Participating Credit Institution.

