

Public Disclosure Authorized

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CREDIT NUMBER 3939-HO

# Development Credit Agreement

(Poverty Reduction Support Technical Assistance Project)

between

REPUBLIC OF HONDURAS

and

INTERNATIONAL DEVELOPMENT ASSOCIATION

Dated September 22, 2004

Public Disclosure Authorized

**CREDIT NUMBER 3939-HO**

**DEVELOPMENT CREDIT AGREEMENT**

AGREEMENT, dated September 22, 2004, between REPUBLIC OF HONDURAS (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;

WHEREAS (B) the Borrower has requested assistance from the United Kingdom's Department for International Development (DFID) in financing Part A.3 of the Project, and from the Swedish International Development Corporation Agency (SIDA) in financing Parts B.1, B.3, C.6 (b) and a portion of Part D of the Project;

WHEREAS (C) DFID and SIDA intend to deposit the assistance referred to in the preceding paragraph in a trust fund to be administered by the Association in accordance with the terms of an administration agreement to be entered into between the Association and each of DFID and SIDA (the Administration Agreements);

WHEREAS (D) by an agreement to be entered into between the Association and the Borrower (the Grant Agreement), the Association intends to make a grant to the Borrower in the amount provided by DFID and SIDA less any operational expenses agreed to with the Association in the Administration Agreements, provided that the Administration Agreements are signed by the parties thereto and said amount is deposited by DFID and SIDA with the Association; and

WHEREAS (E) 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.

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 May 1, 2004) (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) “CONASA” means *Consejo Nacional de Agua y Saneamiento*, the Borrower’s water planning board;

(b) “CPME” means *Comisión Presidencial de Modernización del Estado*, the Borrower’s Presidential Commission for the Modernization of the State established by legislative decree No. 190-91 of December 11, 1991, as a collective body headed by the President of Honduras, responsible for the formulation, study and design of national policies for the reform and improvement of the Honduran State, as well as for the formulation of specialized programs and projects and for the periodic evaluation of results;

(c) “DGSC” means *Dirección General del Servicio Civil*, the Borrower’s Civil Service General Directorate within SDP;

(d) “ERSAPS” means *Ente Regulador de los Servicios de Agua Potable y Saneamiento*, the Borrower’s water sector regulator;

(e) “Financial Monitoring Report” or “FMR” means each report prepared in accordance with Section 4.02 of this Agreement;

(f) “Implementation Letter” means the letter of even date herewith from the Borrower to the Association which sets forth the Project indicators;

(g) “Inter-institutional Arrangements” means the arrangements referred to in Section 3.04 of this Agreement;

(h) “Operational Manual” means the manual referred to in Section 3.03 (a) of this Agreement;

(i) “PCU” means the project coordination unit referred to in Section 3.07 (a) of this Agreement;

(j) “PEU” means each of the project executing units referred to in Section 3.08 (a) of this Agreement;

(k) “Procurement Plan” means the Borrower’s procurement plan, dated May 19, 2004 covering the initial 18 month period (or longer) of Project implementation, as the same shall be updated from time to time in accordance with the provisions of Section 3.02 to this Agreement, to cover succeeding 18 month periods (or longer) of Project implementation;

(l) “PRS” means the Borrower’s Poverty Reduction Strategy, as set forth in the PRSP;

(m) “PRSP” means the Borrower’s Poverty Reduction Strategy Paper as published in Association Report No. 22661 dated September 17, 2001, updated as set forth in the Association Report No. 27648 dated February 2, 2004;

(n) “PSC” means the project steering committee referred to in Section 3.06 of this Agreement;

(o) “PSIA” means poverty and social impact analyses;

(p) “SDP” means *Secretaría de Estado del Despacho Presidencial*, the Borrower’s Ministry of the Presidency;

(q) “SEFIN” means *Secretaría de Estado en el Despacho de Finanzas*, the Borrower’s Ministry of Finance;

(r) “SIAFI” means *Sistema Integrado de Administración Financiera*, the Borrower’s integrated financial management system;

(s) “SIARH” means *Sistema Integrado de Administración de Recursos Humanos*, the Borrower’s integrated human resource system;

(t) “Special Account” means the account referred to in Section 2.02 (b) of this Agreement;

(u) “Subsidiary Agreement” means the Agreement referred to in Section 3.05 (a) of this Agreement;

(v) “SWAp” means sector wide approach, a multi-donor pooled financing mechanism designed to support an entire sector or sub-sector of the Borrower’s public administration;

(w) “TSC” means *Tribunal Superior de Cuentas*, the Borrower’s governing entity for the public resource control system with functional and administrative autonomy, established pursuant to Article 222 of the Borrower’s Constitution (as amended to date);

(x) “UAP” means *Unidad de Administración de Proyectos*, the Borrower’s project management unit under SEFIN; and

(y) “UNAT” means *Unidad de Apoyo Técnico*, the Borrower’s technical unit, operating under the coordination of the SDP and established under Borrower Executive Decree No. PCM-008-97 and governed by Borrower Executive Decree PCM-015-97.

## 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 five million six hundred thousand Special Drawing Rights (SDR 5,600,000).

Section 2.02. (a) 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.

(b) The Borrower may, for the purposes of the Project, open and maintain in Dollars a special deposit account in its Central Bank on terms and conditions satisfactory

to the Association. Deposits into, and payments out of, the Special Account shall be made in accordance with the provisions of Schedule 4 to this Agreement.

Section 2.03. The Closing Date shall be June 15, 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, 2014 and ending June 15, 2044. Each installment to and including the installment payable on June 15, 2024 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. The Borrower declares its commitment to the objectives of the Project as set forth in Schedule 2 to this Agreement, and, to this end, shall:

(a) carry out: (i) Part A of the Project through UNAT with the assistance of CPME; (ii) Part B.1 of the Project through DGSC with the assistance of CPME; (iii) Part B.2 of the Project through UAP, with the assistance of CPME; (iv) Part C of the Project through CPME and any other entity selected by the PSC in accordance with the procedures set forth in the Operational Manual to carry out activities under Part C of the Project; and (v) Part D of the Project through CPME, all with due diligence and efficiency and in conformity with appropriate technical, administrative, financial and environmental practices, and shall provide, promptly as needed, the funds, facilities, services and other resources required for the Project; and

(b) cause TSC to carry out Part B.3 of the Project, with the assistance of CPME, with due diligence and efficiency and in conformity with appropriate technical, administrative and financial practices, and shall provide, promptly as needed, the funds, facilities, services and other resources required for the Project.

Section 3.02. (a) Except as the Association shall otherwise agree, procurement of the goods, non-consultant services 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 3 to this Agreement, as said provisions may be further elaborated in the Procurement Plan.

(b) The Borrower shall update the Procurement Plan in accordance with guidelines acceptable to the Association, and furnish such update to the Association not later than 12 months after the date of the preceding Procurement Plan, for the Association's approval.

Section 3.03. (a) The Borrower shall carry out Parts A, B.1, B.2, C and D of the Project and shall cause TSC to carry out Part B.3 of the Project in accordance with an operational manual, satisfactory to the Association, said manual to include, *inter alia*: (i) the disbursement and procurement procedures to be followed under the Project; (ii) the terms of reference for consultants' services to be carried out during the first year of Project implementation; (iii) the criteria and selection procedures for the provision of technical assistance under Part C of the Project; (iv) the Project's implementation plan; and (v) the composition, functions and responsibilities of the PSC, the PCU and each PEU.



(b) In case of any conflict between the terms of the Operational Manual and those of this Agreement, the terms of this Agreement shall prevail.

Section 3.04. For purposes of carrying out Parts A, B.1, B.2, and C of the Project, the Borrower shall prepare and execute inter-institutional arrangements among CPME, UNAT, DGSC and UAP (the Inter-institutional Arrangements), which shall include, *inter alia*, the functions and responsibilities of: (a) UNAT and CPME under Part A of the Project; (b) DGSC and CPME under Part B.1 of the Project; (c) UAP and CPME under Part B.2 of the Project; and (d) CPME and any other entity selected by the PSC in accordance with the procedures set forth in the Operational Manual to carry out activities under Part C of the Project.

Section 3.05 (a) For purposes of carrying out Part B.3 of the Project, the Borrower shall transfer, on a grant basis, the portion of the proceeds of the Credit allocated for Part B.3 of the Project under an agreement to be entered into between the Borrower and TSC (the Subsidiary Agreement), under terms and conditions satisfactory to the Association, providing, *inter alia*: (i) that TSC shall carry out Part B.3 of the Project in accordance with the terms of this Agreement and of the Operational Manual; and (ii) that TSC shall carry out the obligations set forth in Sections 9.03, 9.04, 9.05, 9.06 and 9.07 of the General Conditions (relating to insurance, use of goods and services, plans and schedules, records and reports and maintenance, respectively, in respect of Part B.3 of the Project).

(b) The Borrower shall exercise its rights under the Subsidiary Agreement in such a 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, terminate, abrogate, waive or fail to enforce the Subsidiary Agreement or any provision thereof.

Section 3.06. The Borrower shall establish and thereafter operate and maintain a Project steering committee (the PSC) to direct the overall management, coordination and supervision of the Project, headed by the Secretary of SDP and including the Secretary of SEFIN and the Executive Secretary of CPME.

Section 3.07. (a) The Borrower shall establish and thereafter operate and maintain within CPME, during the implementation of the Project, a Project coordination unit (the PCU) with functions and responsibilities satisfactory to the Association.

(b) The Borrower shall ensure that the PCU is at all times during the implementation of the Project headed by a coordinator and assisted by staff in adequate numbers, all with qualifications and experience satisfactory to the Association.

Section 3.08. (a) The Borrower shall establish a project executing unit (PEU) in each of UNAT, UAP and DGSC, and shall cause TSC to establish a PEU in TSC to carry out the day-to-day activities under the Project.

(b) The Borrower shall ensure that each of its PEUs, and cause TSC to ensure that TSC's PEU, is at all times during the implementation of the Project headed by a coordinator and assisted by staff in adequate numbers, all with qualifications and experience satisfactory to the Association.

Section 3.09. The Borrower shall:

(a) maintain, and cause TSC to maintain, policies and procedures adequate to enable it to monitor and evaluate on an ongoing basis, in accordance with the indicators set forth in the Implementation Letter, 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, not later than six months after the Effective Date and semestrally thereafter, 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 TSC and the Association, not later than two months after the date of such report, or such later date as the Association shall request, 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.

Section 3.10. 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 to ensure the sustainability of the Project;

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

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

#### **ARTICLE IV**

##### **Financial Covenants**

Section 4.01. (a) The Borrower shall, and shall cause TSC (with respect to Part B.3 of the Project) to, establish and maintain a financial management system, including records and accounts, and prepare financial statements in accordance with consistently applied accounting standards acceptable to the Association, adequate to reflect the operations, resources and expenditures related to the Project.

(b) The Borrower shall, and shall cause TSC (with respect to Part B.3 of the Project) to:

- (i) have the financial statements referred to in paragraph (a) of this Section for each fiscal year (or other period agreed to by the Association), audited, in accordance with consistently applied auditing standards acceptable to the Association, by independent auditors acceptable to the Association;
- (ii) furnish to the Association as soon as available, but in any case not later than four months after the end of each such year (or such other period agreed to by the Association): (A) certified copies of the financial statements referred to in paragraph (a) of this Section for such year (or other period agreed to by the Association), as so audited; and (B) an opinion on such statements by said auditors, in scope and detail satisfactory to the Association; and
- (iii) furnish to the Association such other information concerning such records and accounts, and the audit of such financial statements, and concerning said auditors, as the Association may from time to time reasonably request.

(c) For all expenditures with respect to which withdrawals from the Credit Account were made on the basis of statements of expenditure, the Borrower shall, and shall cause TSC (with respect to Part B.3 of the Project) to:

- (i) retain, until at least one year after the Association has received the audit report for, or covering, the fiscal year in which the last withdrawal from the Credit Account was made, all records (contracts, orders, invoices, bills, receipts and other documents) evidencing such expenditures;
- (ii) enable the Association's representatives to examine such records; and
- (iii) ensure that such statements of expenditure are included in the audit for each fiscal year (or other period agreed to by the Association), referred to in paragraph (b) of this Section.

Section 4.02. (a) Without limitation upon the Borrower's progress reporting obligations set out in Section 3.09 of this Agreement, the Borrower shall, and shall cause TSC (with respect to Part B.3 of the Project) to, prepare and furnish to the Association a financial monitoring report, in form and substance satisfactory to the Association, which:

- (i) sets forth sources and uses of funds for the Project, both cumulatively and for the period covered by said report, showing separately funds provided under the Credit, and explains variances between the actual and planned uses of such funds;
- (ii) describes physical progress in Project implementation, both cumulatively and for the period covered by said report, and explains variances between the actual and planned Project implementation; and
- (iii) sets forth the status of procurement under the Project, as at the end of the period covered by said report.

(b) The first FMR shall be furnished to the Association not later than 45 days after the end of the first calendar quarter after the Effective Date, and shall cover the period from the incurrence of the first expenditure under the Project through the end of such first calendar quarter; thereafter, each FMR shall be furnished to the Association not later than 45 days after each subsequent calendar quarter, and shall cover such calendar quarter.

## **ARTICLE V**

### **Remedies of the Association**

Section 5.01. Pursuant to Section 6.02 (l) of the General Conditions, the following additional event is specified, namely:

(a) Subject to paragraph (b) of this Section, the right of the Borrower to withdraw the proceeds of any grant made to the Borrower for the financing of the Project shall have been suspended, canceled or terminated in whole or in part, pursuant to the terms of the Grant Agreement.

(b) Paragraph (a) of this Section shall not apply if the Borrower establishes to the satisfaction of the Association that: (i) such suspension, cancellation or termination is not caused by the failure of the Borrower to perform any of its obligations under such agreement; and (ii) adequate funds for the Project are available to the Borrower from other sources on terms and conditions consistent with the obligations of the Borrower under this Agreement.

Section 5.02. Pursuant to Section 7.01 (h) of the General Conditions, the following additional event is specified, namely, that the event specified in paragraph (a) of Section 5.01 of this Agreement shall occur, subject to the proviso of paragraph (b) of that Section.

## **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) the Borrower has presented to the Association a satisfactory action plan for Project activities to be completed during the first year of Project implementation;

(b) the Association has approved the Operational Manual and the Procurement Plan (updated as necessary, prior to the conclusion of its original 18-month period, to reflect changes arising between its May 19, 2004 date and the Effective Date, and including the details for the first quarter of Project implementation);

(c) the PSC, the PCU and each PEU have been established and include the necessary technical and administrative staff;

(d) the Subsidiary Agreement and the Inter-institutional Arrangements have been executed and delivered; and

(e) all conditions precedent to effectiveness of the Grant Agreement, or to the right of the Borrower to start making withdrawals thereunder, except only the effectiveness of the Development Credit Agreement, have been fulfilled.

Section 6.02. The following is an additional matter, 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, namely, that the Subsidiary Agreement has been duly authorized or ratified by the Borrower and TSC, and is legally binding upon the Borrower and TSC in accordance with its terms.

Section 6.03. The date December 22, 2004 is hereby specified for the purposes of Section 12.04 of the General Conditions.

## ARTICLE VII

### Representative of the Borrower; Addresses

Section 7.01. The Secretary of SEFIN 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:

*Secretaría de Estado en el Despacho de Finanzas*  
Tegucigalpa, M.D.C.  
Honduras

Cable address:

HACIENDA  
Tegucigalpa

Facsimile:

(504) 237-4142  
(504) 237-5033

For the Association:

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

Cable address:

INDEVAS  
Washington, D.C.

Telex:

248423 (MCI) or  
64145 (MCI)

Facsimile:

(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 Tegucigalpa, Honduras, as of the day and year first above written.

REPUBLIC OF HONDURAS

By /s/ Ralph Oberholzer

Authorized Representative

INTERNATIONAL DEVELOPMENT ASSOCIATION

By /s/ Joseph Owen

Authorized Representative



**SCHEDULE 1**

**Withdrawal of the Proceeds of the Credit**

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) Goods under Parts A.1, A.2, B.2, C.1-C.5, C.6 (a), C.7 and D of the Project	870,000	100% of foreign expenditures and 88% of local expenditures
(2) Consultants' services under Parts A.1, A.2, B.2, C.1-C.5, C.6 (a), C.7 and D of the Project	3,870,000	98%
(3) Communication services under Parts A.1, A.2, B.2, C.1-C.5, C.6 (a), C.7 and D of the Project	30,000	100% of foreign expenditures and 88% of local expenditures
(4) Training/Workshops under Parts A.1, A.2, B.2, C.1-C.5, C.6 (a), C.7 and D of the Project	290,000	100%

<u>Category</u>	<u>Amount of the Credit Allocated (Expressed in SDR Equivalent)</u>	<u>% of Expenditures to be Financed</u>
(5) Incremental Operating Costs under Parts A.1, A.2, B.2, C.1-C.5, C.6 (a), C.7 and D of the Project	250,000	80% until disbursements under this Category have reached an aggregate amount equivalent to SDR 100,000; 60% until disbursements under this Category have reached an aggregate amount equivalent to SDR 200,000; and 40% thereafter
(6) Unallocated	290,000	
TOTAL	<u>5,600,000</u> =====	

2. For the purposes of this Schedule:

(a) the term “communication services” means expenditures for radio, television and printed advertisements incurred by the Borrower in connection with the carrying out of the Project;

(b) 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;

(c) the term “incremental operating costs” means reasonable expenditures which would not have been incurred absent the Project, for the maintenance and leasing of vehicles and equipment, for fuel, office supplies and other consumables, salaries of incremental PCU staff, utilities and travel, transportation and accommodations;

(d) 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

(e) the term “training/workshops” means expenditures (other than for consultants’ services) incurred for: (i) reasonable travel, room, board and *per diem* expenditures incurred by trainers and trainees in connection with their training and by non-consultant training facilitators; (ii) course fees; (iii) training/workshop facility and equipment rentals; (iv) training material preparation, acquisition, reproduction and distribution expenses not otherwise covered under this paragraph; (v) scholarships and fellowships for training courses to be provided in the Borrower’s territory or abroad; and (vi) study tours and internships in the Borrower’s territory or abroad.

3. Notwithstanding the provisions of paragraph 1 above, no withdrawals shall be made in respect of payments made for expenditures prior to the date of this Agreement, except that withdrawals, in an aggregate amount not exceeding the equivalent of SDR 560,000, may be made on account of payments made for expenditures before that date but after May 1, 2004 (but in no case incurred earlier than the twelve months immediately before the date of this Agreement).

4. The Association may require withdrawals from the Credit Account to be made on the basis of statements of expenditure for expenditures under contracts for: (a) goods costing less than \$150,000 equivalent per contract; (b) for services of individual consultants costing less than \$50,000 equivalent per contract; (c) for services of consulting firms under contracts costing less than \$100,000 equivalent per contract; (d) for communication services; (e) training/workshops; and (f) incremental operating costs, all under such terms and conditions as the Association shall specify by notice to the Borrower.

## SCHEDULE 2

### Description of the Project

The objective of the Project is to assist the Borrower in improving its institutional capacity in the areas of planning, public expenditure management, accountability, public administration, public service delivery, and participatory monitoring, thereby facilitating implementation of the PRS.

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: Developing the Borrower's Capacity to Manage, Monitor, Evaluate and Improve PRS Implementation

1. Strengthening UNAT's capacity to analyze and disseminate the results of public programs related to the PRS, including:

(a) establishing a sub-unit within UNAT specifically responsible for preparing studies of the results and impacts of the Borrower's policies related to the PRS;

(b) preparing PSIA in the areas in which the Borrower is introducing new policies to guide decision-making and to provide stakeholders with a deeper understanding of policy issues; and

(c) carrying out an information campaign to disseminate and promote studies on policy initiatives within the PRS framework supported by the Borrower and to promote the results of PSIA related to such initiatives.

2. Strengthening the Borrower's capacity to coordinate foreign assistance, including:

(a) strengthening the capacity of the Borrower to coordinate international cooperation potentially leading to the establishment of SWAps through diagnosing and mapping of existing projects and the alignment and integration of projects and activities; and

(b) developing and disseminating adequate guidelines on SWAps, standardizing administrative procedures and a fiduciary framework.

3. Enhancing the Borrower's PRS consultative process through regular consultations with communities to identify priorities, complemented by stakeholder involvement in designing and implementing the PRS programs, including strengthening the work of the PRS consultative council in monitoring and evaluating PRS implementation, including the perspective from regional and local levels.

Part B: Improving the Implementation of Public Sector Management

1. Implementing the new civil service legislation and continuing efforts to reengineer the public sector, including:

(a) expanding and integrating SIARH with SIAFI, by training personnel and installing the necessary infrastructure to operate the upgraded system;

(b) (i) conceptualizing the structure and functions of the new civil service regulatory office (that will replace the DGSC with additional supervisory and regulatory functions according to the new normative framework); and (ii) acquiring furniture and other equipment necessary for day-to-day operation of the new civil service regulatory office;

(c) training the Borrower's human resources personnel in analysis and classification of positions, recruitment and selection, performance evaluation, professional development, and motivating personnel;

(d) developing studies and providing advisory services to assess the fiscal impact and implications of salary and remuneration schemes for the overall public sector (under the new civil service legislation and the new salary law) to ensure the Borrower's fiscal sustainability;

(e) (i) reengineering the organizational structures of selected pilot entities and carrying out a comprehensive human resources gap analysis for the effective implementation of civil service reforms in such selected pilot entities; and (ii) implementing further e-government strategies; and

(f) (i) evaluating existing personnel and recruitment of new personnel in selected pilot entities to initiate the implementation of the new civil service legislation; and (ii) developing the capacity of the selected pilot entities to apply the new human resources policies regarding classification of positions, recruitment and selection, performance evaluation and professional development.

2. Upgrading and expanding the capacity of SIAFI by developing a set of norms, methodologies and computer-based systems, including:

(a) acquiring software, communications and computer equipment, as well as data links and licenses to use servers for the upgrading and expansion of the internet-based version of SIAFI (e-SIAFI); and

(b) conducting a review of the Borrower's central government principal financial accounts to improve the accuracy and reliability of public financial information.

3. Strengthening the Borrower's institutional capacity to ensure accountability through internal and external control, by assisting TSC to establish stronger financial controls, thereby instituting greater transparency in public financial and non-financial management, including:

(a) training and providing seminars for TSC and internal control units' staff in the monitoring of public debt, probity and ethics, financial audits, evaluation of fiscal accounts, public procurement and other control-related areas; and

(b) acquiring equipment (such as computers and communications) for each area of the TSC.

Part C: Supporting Sectoral Activities within the Framework of the PRS

1. Supporting the implementation of the Borrower's PRS policies in the telecommunications sector with specific activities to be determined by the PSC in accordance with the procedures set forth in the Operational Manual, which could include the following:

(a) restructuring and modernizing the Borrower's telecommunications company (HONDUTEL) to attract a private operator;

(b) preparing new telecommunications legislation; and

(c) strengthening the newly established telecommunications coordinating unit.

2. Supporting the implementation of the Borrower's PRS policies in the power sector with specific activities to be determined by the PSC in accordance with the procedures set forth in the Operational Manual, which could include the following:

(a) improving the efficiency of the Borrower's power company (*Empresa Nacional de Energía Eléctrica*, or ENEE), including its restructuring;

(b) designing the institutional and regulatory reforms necessary to improve the performance of the sector;

(c) carrying out a comprehensive study of power tariffs, as well as of various regulatory aspects of the power sector;

(d) strengthening the Borrower's national commission of energy, which is the entity in charge of regulating the power sector; and

(e) identifying and implementing viable approaches to provide energy services to consumers in rural and semi-urban areas of the Borrower.

3. Supporting the implementation of the Borrower's PRS policies in the ports sector with specific activities to be determined by the PSC in accordance with the procedures set forth in the Operational Manual, which could include the following:

(a) restructuring the Borrower's national ports company;

(b) strengthening the organizational capacity of the Borrower's port regulatory entity in line with the new ports' law (*Ley General de Puertos*); and

(c) supporting efforts to attract private investment for Honduran ports.

4. Supporting the implementation of the Borrower's PRS policies in the water sector with specific activities to be determined by the PSC in accordance with the procedures set forth in the Operational Manual, which could include the following:

(a) supporting CONASA and strengthening ERSAPS;

(b) supporting an information campaign aimed at the general public, non-governmental organizations, municipalities and government in general regarding the reforms introduced by the Borrower's water law passed in 2003; and

(c) acquiring technical equipment (computers and software) to allow ERSAPS to operate efficiently.

5. Supporting the implementation of the Borrower's PRS policies in the environmental sector with specific activities to be determined by the PSC in accordance with the procedures set forth in the Operational Manual, which could include the following:

(a) improving the quality and accuracy of the Borrower's information in the sector;

(b) reviewing the sector's policies and regulatory framework;

(c) carrying out workshops to strengthen the Borrower's capacity to conduct environmental risk assessments; and

(d) carrying out a comprehensive diagnosis of key areas to determine necessary institutional reforms in the sector.

6. Supporting the implementation of the Borrower's PRS policies in the social sectors with specific activities to be determined by the PSC in accordance with the procedures set forth in the Operational Manual, which could include the following:

(a) carrying out a feasibility study to expand the role of local education development associations to cover basic infrastructure, transportation networks, and health issues; and

(b) carrying out a comprehensive teacher allocation post review (*auditoría de puestos*) in the Borrower's departments of Francisco Morazán and Cortés, and possibly other departments thereafter.

7. Supporting the implementation of the Borrower's PRS policies in other sectors with specific activities to be determined by the PSC in accordance with the procedures set forth in the Operational Manual.

#### Part D: Project Management

Provision of technical assistance, equipment, training and incremental operating costs, as necessary, to establish, operate and strengthen the PCU and each PEU to enable such units to effectively coordinate, monitor and evaluate the implementation of the Project components (including audit services for purposes of Section 4.01 of this Agreement).



\* \* \*

The Project is expected to be completed by December 15, 2007.

### **SCHEDULE 3**

#### **Procurement**

##### Section I. General

A. All goods and services (other than consultants' services) shall be procured in accordance with the provisions of Section I of the "Guidelines for Procurement under IBRD Loans and IDA Credits" dated May 2004 (the Procurement Guidelines), and with the provisions of this Schedule.

B. All consultants' services shall be procured in accordance with Sections I and IV of the "Guidelines: Selection and Employment of Consultants by World Bank Borrowers" dated May 2004 (the Consultant Guidelines), and with the provisions of this Schedule.

C. The capitalized terms used below in this Schedule to describe particular procurement methods or methods of review by the Association of particular contracts, have the meanings ascribed to them in the Procurement Guidelines, or Consultant Guidelines, as the case may be.

##### Section II. Particular Methods of Procurement of Goods and Services (other than Consultants' Services)

A. International Competitive Bidding. Except as otherwise provided in Part B of this Section, contracts shall be awarded on the basis of International Competitive Bidding. The provisions of paragraphs 2.55 and 2.56 of the Procurement Guidelines, providing for domestic preference in the evaluation of bids, shall apply to goods manufactured in the territory of the Borrower.

##### B. Other Procurement Procedures

1. National Competitive Bidding. Goods and non-consultant services estimated to cost less than \$150,000 equivalent per contract may be procured under contracts awarded on the basis of National Competitive Bidding and the following additional provisions:

(a) Contracts shall be awarded to the lowest evaluated bid in accordance with criteria set forth in the bidding documents, and without taking into account, in the evaluation, the financial cost of foreign exchange components.

(b) Foreign bidders shall not, as a condition for submitting bids, be required to:

- (i) be registered in Honduras;
- (ii) have a representative in Honduras;
- (iii) be associated with Honduran suppliers or contractors; and
- (iv) certify that, in their country of origin, Honduran suppliers or contractors are allowed to participate in competitive bidding procedures under equal conditions with other bidders.

(c) Contracts shall not be divided for the sole purpose of reducing contract amounts.

2. Shopping. Goods and non-consultant services estimated to cost less than \$25,000 equivalent per contract may be procured under contracts awarded on the basis of Shopping.

3. Direct Contracting. Goods and non-consultant services which the Association agrees meet the requirements for Direct Contracting may be procured in accordance with the provisions of said procurement method.

### Section III. Particular Methods of Procurement of Consultants' Services

A. Quality- and Cost-based Selection. Except as otherwise provided in Part B of this Section, consultants' services shall be procured under contracts awarded on the basis of Quality- and Cost-based Selection. For purposes of paragraph 2.7 of the Consultant Guidelines, the short list of consultants for services estimated to cost less than \$200,000 equivalent per contract may comprise entirely national consultants.

#### B. Other Procedures

1. Least-cost Selection. Services for assignments which the Association agrees meet the requirements of paragraph 3.6 of the Consultant Guidelines may be procured under contracts awarded on the basis of Least-cost Selection in accordance with the provisions of paragraphs 3.1 and 3.6 of the Consultant Guidelines.

2. Selection Based on Consultants' Qualifications. Services estimated to cost less than \$100,000 equivalent per contract may be procured under contracts awarded in accordance with the provisions of paragraphs 3.1, 3.7 and 3.8 of the Consultant Guidelines.

3. Individual Consultants. Services for assignments that meet the requirements set forth in the first sentence of paragraph 5.1 of the Consultant Guidelines may be procured under contracts awarded to individual consultants in accordance with the provisions of paragraphs 5.2 through 5.3 of the Consultant Guidelines. Under the circumstances described in paragraph 5.4 of the Consultant Guidelines, such contracts may be awarded to individual consultants on a sole-source basis, subject to prior approval of the Association.

C. Special Provisions for Selection of Consultants

In addition and without limitation to any other provisions set forth in this Schedule or the Consultant Guidelines, the following principles of procurement shall expressly govern all procurement of consultants' services referred to in Section III of this Schedule:

1. foreign consultants shall be permitted to participate in the selection process, even if there is availability of Honduran consultants for the services being procured; and
2. foreign consultants shall not be required to be registered with Honduran associations or to be associated with Honduran consulting firms as a condition for participating in any selection process.

Section IV. Review by the Association of Procurement Decisions

The Procurement Plan shall set forth those contracts which shall be subject to the Association's Prior Review. All other contracts shall be subject to Post Review by the Association.

## **SCHEDULE 4**

### **Special Account**

1. For the purposes of this Schedule:
  - (a) the term “eligible Categories” means Categories (1) through (5) set forth in the table in paragraph 1 of Schedule 1 to this Agreement;
  - (b) the term “eligible expenditures” means expenditures 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 allocated from time to time to the eligible Categories in accordance with the provisions of Schedule 1 to this Agreement; and
  - (c) the term “Authorized Allocation” means an amount equivalent to \$750,000 to be withdrawn from the Credit Account and deposited into the Special Account pursuant to paragraph 3 (a) of this Schedule.
2. Payments out of the Special Account shall be made exclusively for eligible expenditures in accordance with the provisions of this Schedule.
3. After the Association has received evidence satisfactory to it that the Special Account has been duly opened, withdrawals of the Authorized Allocation and subsequent withdrawals to replenish the Special Account shall be made as follows:
  - (a) For withdrawals of the Authorized Allocation, the Borrower shall furnish to the Association a request or requests for deposit into the Special Account of an amount or amounts which do not exceed the aggregate amount of the Authorized Allocation. On the basis of such request or requests, the Association shall, on behalf of the Borrower, withdraw from the Credit Account and deposit into the Special Account such amount or amounts as the Borrower shall have requested.
  - (b)
    - (i) For replenishment of the Special Account, the Borrower shall furnish to the Association requests for deposits into the Special Account at such intervals as the Association shall specify.
    - (ii) 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 paragraph 4 of this Schedule 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 the 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 the Special Account for eligible expenditures. All such deposits shall be withdrawn by the Association from the Credit Account under the respective eligible Categories, and in the respective equivalent amounts, as shall have been justified by said documents and other evidence.

4. For each payment made by the Borrower out of the 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.

5. Notwithstanding the provisions of paragraph 3 of this Schedule, the Association shall not be required to make further deposits into the Special Account:

(a) if, at any time, the Association shall have determined that all further withdrawals should be made by the Borrower directly from the Credit Account in accordance with the provisions of Article V of the General Conditions and paragraph (a) of Section 2.02 of this Agreement;

(b) 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 the records and accounts for the Special Account;

(c) 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 the provisions of Section 6.02 of the General Conditions; or

(d) once the total unwithdrawn amount of the Credit allocated to the 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 with respect to the Project, shall equal the equivalent of twice the amount of the Authorized Allocation.

Thereafter, withdrawal from the Credit Account of the remaining unwithdrawn amount of the Credit allocated to the eligible Categories 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 the Special Account as of the date of such notice will be utilized in making payments for eligible expenditures.

6. (a) If the Association shall have determined at any time that any payment out of the Special Account: (i) was made for an expenditure or in an amount not eligible pursuant to paragraph 2 of this Schedule; or (ii) was not justified by the evidence furnished to the Association, the Borrower shall, promptly upon notice from the Association: (A) provide such additional evidence as the Association may request; or (B) deposit into the Special Account (or, if the Association shall so request, refund to the Association) an amount equal to the amount of such payment or the portion thereof not so eligible or justified. Unless the Association shall otherwise agree, no further deposit by the Association into the 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 shall have determined at any time that any amount outstanding in the Special Account will not be required to cover further payments for eligible expenditures, 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 paragraphs 6 (a), (b) and (c) of this Schedule shall be credited to the Credit Account for subsequent withdrawal or for cancellation in accordance with the relevant provisions of this Agreement, including the General Conditions.