Financing Agreement

(Second National Water Development Project)

between

REPUBLIC OF MALAWI

and

INTERNATIONAL DEVELOPMENT ASSOCIATION

Dated July 17, 2007
FINANCING AGREEMENT

AGREEMENT dated July 17, 2007, entered into between REPUBLIC OF MALAWI ("Recipient") and INTERNATIONAL DEVELOPMENT ASSOCIATION ("Association"). The Recipient and the Association hereby agree as follows:

ARTICLE I — GENERAL CONDITIONS; DEFINITIONS

1.01. The General Conditions (as defined in the Appendix to this Agreement) constitute an integral part of this Agreement.

1.02. Unless the context requires otherwise, the capitalized terms used in this Agreement have the meanings ascribed to them in the General Conditions or in the Appendix to this Agreement.

ARTICLE II — FINANCING

2.01. The Association agrees to extend to the Recipient, on the terms and conditions set forth or referred to in this Agreement, a grant and a credit (collectively, “Financing”) in the following amounts to assist in financing the project described in Schedule 1 to this Agreement (“Project”):

(a) an amount equivalent to fifteen million Special Drawing Rights (SDR 15,000,000) (“Grant”); and

(b) an amount equivalent to eighteen million, four hundred thousand Special Drawing Rights (SDR 18,400,000) (“Credit”).

2.02. The Recipient may withdraw the proceeds of the Financing in accordance with Section V of Schedule 2 to this Agreement.

2.03. The Maximum Commitment Charge Rate payable by the Recipient on the Unwithdrawn Financing Balance shall be one-half of one percent (1/2 of 1%) per annum.

2.04. The Service Charge payable by the Recipient on the Withdrawn Credit Balance shall be equal to three-fourths of one percent (3/4 of 1%) per annum.

2.05. The Payment Dates are April 15 and October 15 in each year.

2.06. The principal amount of the Credit shall be repaid in accordance with the repayment schedule set forth in Schedule 3 to this Agreement.
2.07. The Payment Currency is the Dollar.

ARTICLE III — PROJECT

3.01. The Recipient declares its commitment to the objectives of the Project and the Program. To this end, the Recipient shall carry out or cause the Project to be carried out in accordance with the provisions of Article IV of the General Conditions and the Project Agreements, as the case may be, as follows: (a) the Ministry of Irrigation and Water Development shall be responsible for overall coordination of Project implementation and for the implementation of Parts C and D of the Project; (b) Part A shall be implemented through the Lilongwe and Blantyre Water Boards; and (c) Part B shall be implemented through the Regional Water Boards.

3.02. Without limitation upon the provisions of Section 3.01 of this Agreement, and except as the Recipient and the Association shall otherwise agree, the Recipient shall ensure that the Project is carried out in accordance with the provisions of Schedule 2 to this Agreement.

ARTICLE IV — REMEDIES OF THE ASSOCIATION

4.01. The Additional Events of Suspension consist of the following:

(a) The Project Implementing Entity’s Legislation has been amended, suspended, abrogated, repealed or waived so as to affect materially and adversely the ability of the Project Implementing Entity to perform any of its obligations under the Project Agreement.

(b) A situation has arisen which shall make it improbable that the Program or a significant part thereof will be carried out.

(c) The LWB and/or the BWB has failed to enter into a Service Contract within eighteen (18) months of the Effective Date.

4.02. The Co-financing Deadline for the effectiveness of each Co-financing Agreement is six (6) months from the Effective Date.

ARTICLE V — EFFECTIVENESS; TERMINATION

5.01. The Additional Conditions of Effectiveness consist of the following:

(a) The Subsidiary Agreements have been executed on behalf of the Recipient and each Project Implementing Entity.

(b) The Recipient has adopted a Program Implementation Manual that is satisfactory to the Association in form and substance.
(c) The Recipient has submitted to the Association an annual work plan and budget for the first year of Project implementation that is satisfactory to the Association in form and substance.

(d) The Recipient has established the Program Management Unit under terms of reference acceptable to the Association with the following key staff with qualifications and experience satisfactory to the Association, and recruited in accordance with the procurement procedures set forth in Section IV of Schedule 2 to this Agreement: Program manager, procurement officer, accountant, and a water supply and sanitation engineer.

5.02. The Additional Legal Matter consists of the following, namely, that each Subsidiary Agreement has been duly authorized or ratified by the Recipient and each Project Implementing Entity and is legally binding upon the Recipient and each Project Implementing Entity in accordance with its terms.

5.03. The Effectiveness Deadline is the date one hundred twenty (120) days after the date of this Agreement.
ARTICLE VI — REPRESENTATIVE; ADDRESSES

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

6.02. The Recipient’s Address is:

Ministry of Finance
P.O. Box 30049
Capital City
Lilongwe 3

Malawi

Cable: Telex: Facsimile:
FINANCE 44407 MI 265-1-789173
Lilongwe

6.03. The Association’s Address is:

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

Cable: Telex: Facsimile:
INDEVAS 248423 (MCI) 1-202-477-6391
Washington, D.C.
AGREED at Lilongwe, Republic of Malawi, as of the day and year first above written.

REPUBLIC OF MALAWI

By /s/ Goodall Gondwe

Authorized Representative

INTERNATIONAL DEVELOPMENT ASSOCIATION

By /s/ Timothy Gilbo

Authorized Representative
SCHEDULE 1

Project Description

The objectives of the Project are to: (a) increase access to sustainable water supply and sanitation services for persons living in cities, towns, villages, and Market Centers within the Recipient’s territory; and (b) improve water resource management at the national level.

The Project consists of the following parts:

Part A: Urban Water Supply and Sanitation

1. Priority Investments

Carrying out of priority urban water supply and sanitation investments, including:

   (a) Blantyre: acquisition of spare parts for water pumps, motors and switch gears for raw and clear water at Walker’s Ferry and Chileka pumping stations; carrying out of urgent rehabilitation and maintenance work to the water distribution network; and acquisition of customer meters for replacement of malfunctioning meters and servicing of outstanding customer water connections.

   (b) Lilongwe: acquisition of spare parts including dam valves, pipes and fittings; and carrying out of urgent rehabilitation and maintenance work to the existing water distribution network.

2. Expansion of Water Services to Un-Served Low Income/Peri-Urban Areas

   (a) Blantyre: carrying out of a baseline survey to determine basic coverage, service levels, and service delivery institutional arrangement options in low income/peri-urban areas; carrying out of pilots of different institutional arrangements for the provision of water supply and sanitation services in low income/peri-urban areas; development and implementation of a sanitation and hygiene promotion program; and expansion of water connections, through the acquisition and installation of pipes, fittings, and water meters.

   (b) Lilongwe: carrying out of a baseline survey to determine basic coverage, service levels, and service delivery institutional arrangement options in low income/peri-urban areas; carrying out of pilots of different institutional arrangements for the provision of water supply and sanitation services in low income/peri-urban areas; development and implementation of a sanitation and hygiene promotion program; and expansion of water connections, through the acquisition and installation of pipes, fittings, and water meters.
3. **Aqueduct Planning**

Carrying out of preliminary designs, and environmental and social impact assessments and associated environmental and resettlement action plans, for an aqueduct to convey raw water to treatment plants in Lilongwe.

**Part B: Town, Market Center, and Rural Piped Water Supply and Sanitation**

1. **Town Water Supply and Sanitation**

   (a) Expansion of water supply and sanitation facilities in towns including Mzuzu, Zomba, Kasungu, Mzimba, Mangochi, Mponela, and Likuni.

   (b) Strengthening the operational efficiency of Regional Water Boards in the planning and delivery of water supply and sanitation services to towns.

2. **Market Center and Rural Piped Water Supply and Sanitation**

   (a) Development of community-managed Market Center and rural piped water supply and sanitation services, through the implementation of Subprojects.

   (b) Strengthening the capacity of: (i) District Assemblies to plan and oversee the management of Market Center and rural piped water supply and sanitation programs; (ii) Water User Associations to plan and manage their water and sanitation facilities; and (iii) local utility operators to operate and maintain water and sanitation facilities.

3. **Capacity Building**

   Provision of training to Regional Water Boards, the PMU and PIU staff, District Assemblies and local communities.

**Part C: Water Resource Management**

1. **Enabling Legislation for National Water Policy**

   Development of the water resource management institutional framework through the formulation of enabling legislation for the implementation of the Recipient’s national water policy (2005).

2. **Water Resources Investment Strategy**

   Development of an integrated water resources investment strategy, including feasibility studies, preliminary designs, and environmental and social assessments for priority investments.
3. **Lake Malawi Level Control**

   Strengthening the Recipient’s capacity to regulate the level of Lake Malawi through: (a) preparation of design work for the upgrading of the Kamuzu barrage in Liwonde; (b) preparation of a preliminary design of a low flow pumping barrage at Samama/Mponda; and (c) carrying out any necessary environmental and social impact assessments and consultations with stakeholders, including riparian countries, and preparation of environmental management plans and resettlement action plans, as required.


   Strengthening the Recipient’s water resource management institutional capacity through: (a) the establishment and operationalisation of a national water resources authority; (b) provision of technical advisory services for the establishment of a water resources fund; (c) establishment of a water resources revenue management information system; and (d) carrying out of a licensing reform campaign to both increase revenue collection rates on existing licenses and issue licenses to unlicensed water providers.

5. **Future Water Sources Development**

   Carrying out of feasibility studies, detailed designs, and environmental and social impact assessments and associated environmental and resettlement action plans, for the development of future water sources.

**Part D: Sector Management**

1. **Management of Sector Program**

   Strengthening the capacity of MIWD to manage the Program and Project in areas including sector investment planning, financial management, procurement, Program management, donor coordination, monitoring and evaluation, and information technology and communications.

2. **Strategic Sanitation Plan**

   Development of a comprehensive sanitation plan for the cities of Lilongwe and Blantyre for the operationalisation of the Recipient’s national sanitation policy.

3. **Implementation of a Reform Framework in Urban Water Service Delivery**

   (a) Development and implementation of an institutional and legal framework for private sector participation in the delivery of urban water and sanitation services.
(b) Carrying out of a public awareness campaign on proposed urban water sector reforms, through the implementation of a communications strategy, and holding of consultative workshops among policy makers, utilities staff, civil society, and members of the public.
SCHEDULE 2

Project Execution

Section I. Institutional Arrangements

A. Program Steering Board

(1) **Composition.** The Recipient shall maintain at all times during Project implementation a Program Steering Board. Without limitation to the foregoing, the Program Steering Board shall be chaired by the Chief Secretary, Office of the President and Cabinet, and have membership that includes representatives from the Ministry of Finance; the Ministry of Economic Planning and Development; the Ministry of Justice; the Ministry of Mines, Natural Resources, and Environment; the Ministry of Local Government and Rural Development; the Ministry of Lands, Housing and Surveys; MIWD; Council for Non-Governmental Organizations of Malawi; Malawi Confederation of Chambers of Commerce and Industry; University of Malawi; and Mzuzu University.

(2) **Role.** The Program Steering Board shall be responsible for providing overall oversight and policy guidance under terms of reference that are acceptable to the Association.

B. Program Task Force

(1) **Composition.** The Recipient shall maintain at all times during Project implementation a Program Task Force with a composition that is satisfactory to the Association. Without limitation to the foregoing, the Program Task Force shall comprise mainly representatives of the Key Implementing Entities.

(2) **Role.** The Program Task Force shall be responsible for activities that include the following: (a) the preparation of annual work plans and budgets; (b) monitoring the implementation of annual work plans and utilization of budgets, and making and communicating decisions made on any necessary adjustments required to improve implementation; (c) reviewing terms of reference and work products delivered from consultancies undertaken under the Project; and (d) coordinating the implementation of the Project by the Key Implementing Entities and the Participating Agencies.
C. Project Staffing

(1) Program Management Unit

(a) Staffing. The Recipient shall recruit, as part of the PMU, a water resources management specialist, community participation specialist, and a water reforms specialist within six months of the Effective Date, all under terms of reference and with qualifications and experience, that are satisfactory to the Association, in accordance with the procurement procedures set forth in Section IV of Schedule 2 to this Agreement.

(b) Composition. Except as otherwise provided in this Agreement, the Recipient shall maintain at all times during Project implementation the PMU adequately staffed with persons with qualifications, experience, and terms of reference, that are satisfactory to the Association, including a Program manager, procurement officer, accountant, water supply and sanitation engineer, water resources management specialist, a community participation specialist, and a water reforms specialist.

(c) Role. The PMU shall be responsible for overseeing and coordinating day-to-day implementation of the Project. Without limitation to the foregoing, the PMU shall carry out tasks that shall include: (i) financial management, including preparation of Interim Unaudited Financial Reports for the Project; (ii) preparation of Project Reports; (iii) carrying out procurement for Parts C and D of the Project, Project procurement planning, quality assurance on the procurement systems of the LWB, BWB, and RWBs, and monitoring and reporting on Project procurement progress; (iv) coordinating and accounting for the use of Project funds; (v) establishing a monitoring and evaluation system; (vi) coordinating Project implementation review meetings; (vii) provision of secretariat services to the Program Steering Board and Task Force; and (viii) overseeing the urban water sector reform process.

2. Project Implementation Units

(a) Composition. The Recipient shall maintain or cause to be maintained at all times during Project implementation the PIUs adequately staffed with persons with qualifications, experience, and terms of reference, that are satisfactory to the Association, including a procurement officer, accountant, and water supply and sanitation engineer.

(b) Role. The PIUs shall be responsible for overseeing and coordinating day-to-day implementation of their Respective Parts of the Project. Without limitation to the foregoing, the PIUs shall carry out tasks that shall include the following for their Respective Parts of the Project: (i) financial management, including provision to the PMU of all such information
as it shall require for the preparation of Interim Unaudited Financial Reports for the Project; (ii) provision of all such information as the PMU shall require for the preparation of Project Reports; (iii) carrying out of procurement; and (iv) supervision of consultants and construction activities.

3. **Participating Agencies**

   The Recipient shall ensure that competent staff are designated to work on the Project in all the Participating Agencies, and shall cause the said Agencies to liaise, as necessary, with the Key Implementing Entities and the Program Task Force.

**Section II. Implementation Arrangements**

**A. Subsidiary Agreement**

1. To facilitate the carrying out of the Project Implementing Entity’s Respective Part of the Project, the Recipient shall make part of the proceeds of the Financing available to the Project Implementing Entity under a Subsidiary Agreement between the Recipient and the Project Implementing Entity, under terms and conditions approved by the Association, which shall include the following:

   (a) implementation by the Project Implementing Entity of its Respective Part of the Project in accordance with the terms of this Agreement;

   (b) the requirement that the Project Implementing Entity maintain the PIU with competent staff to undertake all Project related activities, including, without limitation, a procurement officer, accountant, and water supply and sanitation engineer;

   (c) the requirement that the Project Implementing Entity is represented on the Project Task Force throughout Project implementation;

   (d) the requirement that the Project Implementing Entity liaise, as necessary, during Project implementation with the other Key Implementing Entities and Participating Agencies;

   (e) the requirement that the Project Implementing Entity comply with all environmental and social safeguards as provided in the Environmental and Social Management Framework and the Resettlement Policy Framework, including without limitation, the preparation of ESMPs and RAPs, as necessary;
the requirement that the Project Implementing Entity implements its Respective Part of the Project in accordance with the PIM;

an undertaking by the Recipient to pay or cause to be paid to the Project Implementing Entity any outstanding water bills by a public institution by December 31, 2008, and thereafter to ensure the timely payment of dues;

sub-loan and sub-grant terms and conditions; and

an undertaking by the Project Implementing Entity to meet its operations and maintenance costs fully by its 2008/9 fiscal year from revenues collected, and in addition, its depreciation and debt service obligations, by its 2011/12 fiscal year.

2. The Recipient shall exercise its rights under the Subsidiary Agreement in such manner as to protect the interests of the Recipient and the Association and to accomplish the purposes of the Financing. Except as the Association shall otherwise agree, the Recipient shall not assign, amend, abrogate or waive the Subsidiary Agreement or any of its provisions.

B. Program Implementation Manual

The Recipient shall carry out or cause the Project to be carried out in accordance with the PIM, and except as the Association shall otherwise agree, shall not amend, abrogate or waive any provision of the PIM.

C. Annual Work Plans and Budgets

The Recipient shall submit or cause to be submitted to the Association for its review and approval an annual work plan and budget on or about September 30 of each year of Project implementation. The Recipient shall implement or cause to be implemented, the activities reflected in such annual work plans in a manner that is satisfactory to the Association.

D. Environmental and Social Safeguards

1. The Recipient shall at all times carry out or cause the Project to be carried out in accordance with the ESMF and the RPF, and wherever applicable, prepare and implement or cause to be prepared and implemented ESMP(s) and RAP(s).

2. The Recipient shall not amend or waive, or permit to be amended or waived, the ESMF, RPF, ESMP(s) and RAP(s), or any provision thereof.

3. The Recipient shall ensure that the Ministry of Mines, Natural Resources, and Environment and the Ministry of Lands, Housing, and Surveys provide all such
services as shall be required to ensure that the Project is implemented in accordance with the provisions of the ESMF and the RPF, respectively.

E. Expansion of Water Services to Un-Served Low Income/Peri-Urban Areas under Part A.2 of the Project using the Output-Based Approach

1. The Lilongwe and Blantyre Water Boards may use the output based approach in the expansion of water services to the un-served low income/peri-urban areas. In cases where the output-based approach is utilized, the investment costs shall be pre-financed by the said Water Boards or by water services operators, in cases where the said Water Boards deem fit to use the services of the said operators who must have been competitively selected in accordance with the Association’s procurement procedures, as set forth in Section IV of Schedule 2 to this Agreement.

2. The investment costs to the said Water Boards or water services operators, as the case may be, shall be reimbursed, on a periodic basis, at a pre-determined cost per connection that has been found by the Association to meet a reasonable standard of economy and efficiency.

3. The Lilongwe and Blantyre Water Boards shall keep or cause to be kept all documentation on the expenditures underlying the outputs to enable the amounts disbursed to be compared with actual expenditures.

4. The Lilongwe and Blantyre Water Boards shall carry out or cause to be carried out all procurements in accordance with the Association’s procurement procedures, as set forth in Section IV of Schedule 2 to this Agreement.

5. Prior to any payments being made, verification shall be undertaken by an independent expert that is satisfactory to the Association, to establish, without limitation: (a) that the proposed works have been completed in accordance with agreed connection specifications and that service delivery has been satisfactory to the connected households; (b) the actual costs incurred for the underlying outputs; (c) that the Association’s procurement procedures were used as set forth in Section IV of Schedule 2 to this Agreement; and (d) implementation was undertaken in accordance with the ESMF and RPF.

F. Town Investments under Part B.1 of the Project

1. Each Regional Water Board shall develop proposed business plans and investment proposals for individual towns in a consultative manner, and meet the requisite economic, technical, financial, environmental and social standards set forth in the PIM. Without limitation on the foregoing, the Regional Water Board shall ensure that the town business plans are comprehensive setting out inter alia: a proposed tariff structure towards full cost recovery; sound
systems for financial and operations management; adequate implementation capacity; an analysis showing that the proposed investment(s) are cost effective and financially viable; and details of any proposed usage of the output-based approach.

2. The Regional Water Board shall submit the town business plans and investment proposals to MIWD for its appraisal and endorsement, taking into account eligibility criteria set forth in the PIM including, without limitation, a business plan with projected cash flow meeting recurrent costs including operations and maintenance, renewal and replacement of short life assets, and a proportion of expansion costs; effective accounting, financial management, billing/collection, and monitoring and evaluation systems; decentralized day to day management; procurement readiness; and confirmation that the environmental and social impacts of the proposed town investments have been addressed in accordance with the ESMF and RPF, and the applicable laws of the Recipient relating to health, safety and environmental protection.

3. Town investments shall be financed either through the provision of sub-grants or sub-loans under terms and conditions agreed with the Association and set forth in the PIM. Without limitation on the foregoing, a positive list of items eligible for sub-grant financing shall be provided in the PIM, including, without limitation, investments, such as yard taps and public standpipes financed using the output-based approach, and sanitation activities. The MIWD and the Regional Water Board shall enter into a written agreement(s) that is satisfactory to the Association with respect to the proposed investments.

4. In cases where the output-based approach is utilized:
   
   (a) the investment costs shall be pre-financed by the Regional Water Boards or by the water services operators, in cases where the said Regional Water Boards deem fit to use the services of the said operators who must have been competitively selected in accordance with the Association’s procurement procedures, as set forth in Section IV of Schedule 2 to this Agreement;

   (b) the investment costs to the Regional Water Boards or water services operators, as the case may be, shall be reimbursed, on a periodic basis, at a pre-determined cost per connection that has been found by the Association to meet a reasonable standard of economy and efficiency;

   (c) the Regional Water Boards shall keep or cause to be kept all documentation on the expenditures underlying the outputs to enable the amounts disbursed to be compared with actual expenditures;
(d) the Regional Water Boards shall carry out or cause to be carried the activities in accordance with the Association’s procurement procedures, as set forth in Section IV of Schedule 2 to this Agreement; and

(e) an independent verification shall be taken by an independent expert that is satisfactory to the Association, to establish, without limitation, that: (i) the proposed works have been completed in accordance with agreed connection specifications and that service delivery has been satisfactory to the connected households; (ii) the actual costs incurred for the underlying outputs; (iii) the Association’s procurement procedures were used as set forth in Section IV of Schedule 2 to this Agreement; and (iv) implementation was undertaken in accordance with the ESMF and RPF.

G. Subprojects under Part B.2 of the Project

1. The MIWD shall, in consultation with the Regional Water Boards, District Assemblies, and local communities, select participating Market Centers taking into account factors set out in greater detail in the PIM, including, without limitation, socio-economic potential, the District infrastructure plan’s priorities, population levels, existing water and sanitary service levels, and existing electricity supply.

2. To be eligible for Subproject financing under the Project, the District Assembly shall submit an application to the RWB, on behalf of a proposed Subproject Beneficiary, and work closely with the RWB and the proposed Subproject Beneficiary, to meet the various eligibility criteria set out at each stage of the process as set out in the PIM, including, without limitation:

(a) establishing Water User Associations;

(b) hiring a local utility operator and core operating staff, subject to operator performance agreements; and

(c) carrying out pre-feasibility studies, baseline surveys and assessments; and preparing preliminary designs, business plans, sanitation plans, and water supply facilities design and tender documents.

3. An appraisal committee, with representatives from MIWD, RWB and the District Assembly, shall evaluate whether or not a proposed Subproject Beneficiary has met the requirements at each stage of the process.

4. The Regional Water Boards shall:

(a) contract on behalf of the Subproject Beneficiary and shall ensure that proper records are kept reflecting the operations, resources and expenditures
relating to each Subproject in accordance with sound accounting practices that are acceptable to the Association;

(b) ensure that the Subprojects are implemented with due diligence and efficiency and in accordance with sound technical, financial, managerial, social, and environmental standards and practices;

(c) address all the environmental and social impacts of the proposed Subprojects in accordance with the provisions of the ESMF and RPF;

(d) ensure that the proposed Subprojects are in compliance with the standards set forth in the applicable laws and regulations of the Recipient relating to health, safety and environmental protection; and

(e) ensure that the proposed Subprojects have an adequate management and sustainability plan.

5. Training shall be provided, as necessary, by the Regional Water Boards to build the capacity of the Water User Associations and local utility operators in areas including financial management, billing and collection, operating procedures, and monitoring and evaluation.

H. Sector Management under Part D of the Project

The Recipient shall complete the development of a regulatory framework for the delivery of urban water and sanitation services that is satisfactory to the Association within eighteen (18) months of the Effective Date.

Section III. Project Monitoring, Reporting and Evaluation

A. Project Reports

1. (a) The Recipient shall monitor and evaluate the progress of the Project and prepare Project Reports in accordance with the provisions of Section 4.08 of the General Conditions and on the basis of the indicators set forth below in sub-paragraph (b) of this paragraph. Each Project Report shall cover the period of one calendar quarter, and shall be furnished to the Association not later than forty-five (45) days after the end of the period covered by such report.
(b) The performance indicators referred to above in sub-paragraph (a) consist of the following:

<table>
<thead>
<tr>
<th>Performance Indicators</th>
<th>Target Closing Date</th>
</tr>
</thead>
<tbody>
<tr>
<td>Number of people with new or improved water supply</td>
<td>0.4 million new</td>
</tr>
<tr>
<td></td>
<td>0.6 million improved</td>
</tr>
<tr>
<td>Number of people with improved sanitation</td>
<td>0.4 million</td>
</tr>
</tbody>
</table>

**Part A. Blantyre and Lilongwe Water Supply and Sanitation**

| Number of new connections                                 | 7,500                        |
| Number of rehabilitated connections                      | 2,500                        |
| Hours per day of supply, based on weighted average of connections | 20                           |
| Ratio of operating revenues/expenses                     | 1.1                          |

**Part B. Town, Market Center, and Rural Piped Water Supply and Sanitation**

| Number of new connections                                 | 13,500                       |
| Number of rehabilitated connections                      | 30,000                       |
| Hours per day of supply based on weighted average connections | 24                           |
| Ratio of operating revenues/expenses                     | 1.1                          |

**Part C. Water Resources Management**

- National water resources authority established
- Water resources investment strategy prepared
- Level control design and environmental/social safeguards completed

**Part D. Sector Management**

- Program management system in place in MIWD
- Service Contract signed
- Regulatory and institutional framework for urban water supply established
Without limitation on the provisions of sub-paragraph (a) above, the Recipient shall carry out jointly with the Association a comprehensive mid-term review to assess the status of Project implementation, including without limitation, the operations of the BWB and LWB under the proposed Service Contract, and environmental and social management, on or about twenty-four (24) months after the Effective Date. The Recipient shall not later than one month before such review prepare and furnish to the Association a report that is satisfactory to the Association in scope and detail for purposes of such review.

B. Financial Management, Financial Reports and Audits

1. The Recipient shall maintain or cause to be maintained a financial management system in accordance with the provisions of Section 4.09 of the General Conditions.

2. Without limitation on the provisions of Part A of this Section, the Recipient shall prepare and furnish to the Association as part of the Project Report not later than forty-five (45) days after the end of each calendar quarter, an Interim Unaudited Financial Report for the Project covering the quarter, in form and substance satisfactory to the Association.

3. The Recipient shall have its Financial Statements audited in accordance with the provisions of Section 4.09 (b) of the General Conditions. Each audit of the Financial Statements shall cover the period of one fiscal year of the Recipient, commencing with the fiscal year in which the first withdrawal under the Project Preparation Advance was made. The audited Financial Statements for each such period shall be furnished to the Association not later than six months after the end of such period.

Section IV. Procurement

A. General

1. Goods and Works. All goods and works required for the Project and to be financed out of the proceeds of the Financing shall be procured in accordance with the requirements set forth or referred to in Section I of the Procurement Guidelines, and with the provisions of this Section.

2. Consultants’ Services. All consultants’ services required for the Project and to be financed out of the proceeds of the Financing shall be procured in accordance with the requirements set forth or referred to in Sections I and IV of the Consultant Guidelines, and with the provisions of this Section.
Definitions. The capitalized terms used below in this Section to describe particular procurement methods or methods of review by the Association of particular contracts, refer to the corresponding method described in the Procurement Guidelines, or Consultant Guidelines, as the case may be.

B. Particular Methods of Procurement of Goods and Works

1. International Competitive Bidding. Except as otherwise provided in paragraph 2 below, goods and works shall be procured under contracts awarded on the basis of International Competitive Bidding.

2. Other Methods of Procurement of Goods and Works. The following table specifies the methods of procurement, other than International Competitive Bidding, which may be used for goods and works. The Procurement Plan shall specify the circumstances under which such methods may be used:

<table>
<thead>
<tr>
<th>Procurement Method</th>
</tr>
</thead>
<tbody>
<tr>
<td>(a) Limited International Bidding</td>
</tr>
<tr>
<td>(b) National Competitive Bidding</td>
</tr>
<tr>
<td>(c) Shopping</td>
</tr>
<tr>
<td>(d) Direct Contracting</td>
</tr>
<tr>
<td>(e) Force Account</td>
</tr>
</tbody>
</table>

C. Particular Methods of Procurement of Consultants’ Services

1. Quality- and Cost-based Selection. Except as otherwise provided in paragraph 2 below, consultants’ services shall be procured under contracts awarded on the basis of Quality and Cost-based Selection.

2. Other Methods of Procurement of Consultants’ Services. The following table specifies methods of procurement, other than Quality and Cost-based Selection, which may be used for consultants’ services. The Procurement Plan shall specify the circumstances under which such methods may be used:

<table>
<thead>
<tr>
<th>Procurement Method</th>
</tr>
</thead>
<tbody>
<tr>
<td>(a) Selection Based on Consultant Qualifications</td>
</tr>
<tr>
<td>(b) Least Cost Selection</td>
</tr>
<tr>
<td>(c) Fixed Budget Selection</td>
</tr>
</tbody>
</table>
D. Review by the Association of Procurement Decisions

Except as the Association shall otherwise determine by notice to the Recipient, the following contracts shall be subject to Prior Review by the Association:
(a) each contract for goods estimated to cost the equivalent of $250,000 or more;
(b) each contract for works estimated to cost the equivalent of $500,000 or more;
(c) each contract for goods or works procured under Direct Contracting;
(d) each contract for consultant services provided by a firm estimated to cost the equivalent of $100,000 or more;
(e) each contract for consultant services provided by an individual estimated to cost the equivalent of $50,000 or more;
and (f) each contract for consultant services provided by a firm or an individual procured under Single Source Selection. All other contracts shall be subject to Post Review by the Association.

Section V. Withdrawal of the Proceeds of the Financing

A. General

1. The Recipient may withdraw the proceeds of the Financing in accordance with the provisions of Article II of the General Conditions, this Section, and such additional instructions as the Association shall specify by notice to the Recipient (including the “World Bank Disbursement Guidelines for Projects” dated May 2006, as revised from time to time by the Association and as made applicable to this Agreement pursuant to such instructions), to: (a) repay the Project Preparation Advance in accordance with Section 2.07 of the General Conditions; and (b) finance Eligible Expenditures, as set forth in the table in paragraph A.2 below.
2. The following table specifies the categories of Eligible Expenditures that may be financed out of the proceeds of the Financing (“Category”), the allocations of the amounts of the Financing to each Category, and the percentage of expenditures to be financed for Eligible Expenditures in each Category:

<table>
<thead>
<tr>
<th>Category</th>
<th>Amount of the Credit Allocated (Expressed in SDR)</th>
<th>Amount of the Grant Allocated (Expressed in SDR)</th>
<th>Percentage of Expenditures to be Financed (Inclusive of Taxes)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Works and Goods</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>(a) Part A</td>
<td>1,860,000</td>
<td>2,490,000</td>
<td>100%</td>
</tr>
<tr>
<td>(b) Part B</td>
<td>6,260,000</td>
<td>4,880,000</td>
<td></td>
</tr>
<tr>
<td>(c) Part C</td>
<td>260,000</td>
<td>210,000</td>
<td></td>
</tr>
<tr>
<td>(d) Part D</td>
<td>250,000</td>
<td>200,000</td>
<td></td>
</tr>
<tr>
<td>2. Consultants’ Services</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>(a) Part A</td>
<td>210,000</td>
<td>170,000</td>
<td>100%</td>
</tr>
<tr>
<td>(b) Part B.1</td>
<td>1,230,000</td>
<td>1,000,000</td>
<td></td>
</tr>
<tr>
<td>(c) Part C</td>
<td>4,800,000</td>
<td>2,730,000</td>
<td></td>
</tr>
<tr>
<td>(d) Part D</td>
<td>1,100,000</td>
<td>780,000</td>
<td></td>
</tr>
<tr>
<td>3. Subprojects Under Part B.2 of the Project</td>
<td>1,120,000</td>
<td>920,000</td>
<td>100% of amounts disbursed</td>
</tr>
<tr>
<td>4. Training</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>(a) Part B</td>
<td>380,000</td>
<td>310,000</td>
<td>100%</td>
</tr>
<tr>
<td>(b) Part D</td>
<td>130,000</td>
<td>100,000</td>
<td></td>
</tr>
<tr>
<td>5. Operating Costs</td>
<td>490,000</td>
<td>400,000</td>
<td>100%</td>
</tr>
<tr>
<td>6. Refund of Project Preparation Advance</td>
<td>-</td>
<td>600,000</td>
<td>Amount payable pursuant to Section 2.07 of the General Conditions</td>
</tr>
<tr>
<td>7. Unallocated</td>
<td>310,000</td>
<td>210,000</td>
<td></td>
</tr>
</tbody>
</table>

TOTAL: 18,400,000

B. Withdrawal Conditions; Withdrawal Period

1. Notwithstanding the provisions of Part A of this Section, no withdrawal shall be made for payments made prior to the date of this Agreement, except that
withdrawals up to an aggregate amount not to exceed SDR4,340,000 ($6,515,000 equivalent), may be made for payments made prior to this date but on or after June 30, 2006, for Eligible Expenditures under Category 1 (a).

2. The Closing Date is October 31, 2012.

Section VI. Other Undertakings

1. Outstanding Water Bills

The Recipient undertakes to pay or cause to be paid to the respective Project Implementing Entity any outstanding water bills by a public institution by December 31, 2008, and thereafter to ensure the timely payment of any dues.

2. Cost Recovery

The Recipient shall cause the Project Implementing Entity to meet its operations and maintenance costs fully by its 2008/9 fiscal year from revenues collected, and, in addition, its depreciation and debt service obligations, by its 2011/12 fiscal year.
SCHEDULE 3

Repayment Schedule

<table>
<thead>
<tr>
<th>Date Payment Due</th>
<th>Principal Amount of the Credit repayable (expressed as a percentage)*</th>
</tr>
</thead>
<tbody>
<tr>
<td>On each April 15 and October 15</td>
<td></td>
</tr>
<tr>
<td>commencing October 15, 2017, to and including April 15, 2027</td>
<td>1%</td>
</tr>
<tr>
<td>commencing October 15, 2027, to and including April 15, 2047</td>
<td>2%</td>
</tr>
</tbody>
</table>

* The percentages represent the percentage of the principal amount of the Credit to be repaid, except as the Association may otherwise specify pursuant to Section 3.03 (b) of the General Conditions.
APPENDIX

Definitions

1. “Affected Persons” means persons who, on account of the execution of the Project had or would have their: (a) standard of living adversely affected; or (b) right, title, interest in any house, land (including premises, agricultural and grazing land) or any other fixed or movable asset acquired or possessed, temporarily or permanently; or (c) access to productive assets adversely affected, temporarily or permanently; or (d) business, occupation, work or place of residence or habitat adversely affected.

2. “Blantyre Water Board” or “BWB” means the Board established under the Waterworks Act of 1995, Chapter 72:01 of the laws of the Recipient, to provide water supply and water-borne sanitation services in Blantrye, and includes any successor thereto.

3. “Category” means a category set forth in the table in Section V of Schedule 2 to this Agreement.

4. “Co-financier” means, the European Union and the European Investment Bank, referred to in paragraph 10 of the Appendix to the General Conditions, and “Co-financiers” shall mean the European Union and the European Investment Bank, collectively.

5. “Co-financing” means an amount equivalent to twenty million Dollars ($20,000,000), to be provided by each Co-financier to assist in financing the Program.

6. “Co-financing Agreement” means the agreement to be entered into between the Recipient and each Co-financier providing for the Co-financing.


8. “District” means a local government area established pursuant to the Regional and District Boundaries and Place Names Act, Chapter 18:04 of the laws of the Recipient.

9. “District Assembly” means an assembly established pursuant to Section 5 of the Local Government Act, Chapter 22:01 of the laws of the Recipient.

10. “Environmental and Social Management Framework” or “ESMF” means the framework dated, March 2007, prepared by the Recipient and approved by the Association, setting forth an environmental and social screening process that will enable Project implementers to identify and assess potential adverse
environmental and social impacts, and offset and reduce them to acceptable levels, or enhance positive impacts, and in accordance with which ESMPs will be prepared and submitted to the Association for its approval, as the same may be amended from time to time with the concurrence of the Association.

11. “Environmental and Social Management Plan” or “ESMP” means an environmental and social management plan, to be prepared by the Recipient in accordance with the provisions of the ESMF and approved by the Association, setting out measures to mitigate any adverse environmental and social impacts arising from activities to be implemented under the Project, and “Environmental and Social Management Plans” or “ESMPs” shall mean such Environmental and Social Management Plans, collectively.


13. “Interim Unaudited Financial Report” means a report describing progress in Project implementation which: (a) sets forth the sources and uses of funds for the Project, both cumulatively and for the period covered by the said report, and explains variances between the actual and planned uses of such funds; (b) describes physical progress in Project implementation, both cumulatively and for the period covered by the said report, and explains variances between the actual and planned Project implementation; and (c) sets forth the status of procurement under the Project, as at the end of the period covered by the said report.

14. “Key Implementing Entities” means MIWD, BWB, LWB, Northern Region Water Board, Southern Region Water Board and the Central Region Water Board, and includes any successor to each individual Key Implementing Entity.

15. “Lilongwe Water Board” or “LWB” means the Board established under the Recipient’s Waterworks Act of 1995, Chapter 72:01 of the laws of the Recipient, to provide water supply and water-borne sanitation services in Lilongwe, and includes any successor thereto.

16. “Market Center” means a concentrated area of commercial activity, including surrounding local communities and public institutions.

17. “Ministry of Irrigation and Water Development” or “MIWD” means the Recipient’s Ministry with responsibility for irrigation and water development, and includes any successor thereto.

18. “Operating Costs” means the incremental operating costs arising under the Project on account of Project coordination, implementation, and monitoring activities undertaken by the PMU, including salaries of contractual staff, office
equipment, motor vehicle operations and maintenance, and Program management workshops, but excluding salaries of the Recipient’s civil servants.

19. “Participating Agencies” means the Ministry of Mines, Natural Resources, and Environment; the Ministry of Lands, Housing, and Surveys; the Ministry of Justice; the Ministry of Local Government and Rural Development; the Ministry of Economic Planning and Development; the National Council on the Environment; and the Privatization Commission, and includes any successor to each individual Participating Agency.


21. “Procurement Plan” means the Recipient’s procurement plan for the Project, dated March 30, 2007, and referred to in paragraph 1.16 of the Procurement Guidelines and paragraph 1.24 of the Consultant Guidelines, as the same shall be updated from time to time in accordance with the provisions of said paragraphs.

22. “Program” means the Recipient’s National Water Development Program designed to provide water supply and sanitation serves in villages, towns and cities, and to improve water resources management, as set forth or referred to in the letter dated March 23, 2007, from the Recipient to the Association.

23. “Program Implementation Manual” or “PIM” means the Manual specifying, inter alia, the procedures for procurement, disbursement, financial management, accounting, reporting, monitoring and evaluation, environmental and social management, and other implementation arrangements agreed upon by the Recipient and the Association, as the same may be amended from time to time with the approval of the Association, and such term includes any annexes to the said manual.

24. “Program Management Unit” or “PMU” means the Unit established within MIWD with a composition and role described in paragraph C.1 of Section I of Schedule 2 to this Agreement.

25. “Program Steering Board” means the Board with a composition and role described in paragraph A.1 and A.2 of Section I of Schedule 2 to this Agreement.

26. “Program Task Force” means the Task Force with a composition and role described in paragraph B.1 and B.2 of Section I of Schedule 2 to this Agreement.

27. “Project Implementing Entity” means, individually, BWB, LWB, the Northern Region Water Board, the Southern Region Water Board, and the Central Region Water Board, as the case may be.

“Program Implementation Unit” or “PIU” means the Unit established within BWB, LWB and each of the Regional Water Boards with a composition and role described in paragraph C.2 of Section I of Schedule 2 to this Agreement and “Program Implementation Units” or “PIUs” shall mean such Units, collectively.

“Program Preparation Advance” means the advance referred to in Section 2.07 of the General Conditions, granted by the Association to the Recipient pursuant to the letter agreement signed on behalf of the Association on July 17, 2006, and on behalf of the Recipient on July 19, 2006.

“Regional Water Board” or “RWB” means a Board established under the Waterworks Act of 1995, Chapter 72:01 of the laws of the Recipient, to provide water supply and water-borne sanitation services in its respective designated water areas in Malawi, and for purposes of this Agreement means, individually, the Northern Region Water Board, the Central Region Water Board and the Southern Region Water Board, as the case may be, and includes any successor thereto, and Regional Water Boards shall mean such Regional Water Boards, collectively.

“Resettlement Action Plan” or “RAP”, means a plan approved by the Association, to be prepared in accordance with the provisions of the RPF, setting forth principles and procedures governing land acquisition or other associated Project impacts, resettlement and compensation of Affected Persons, as well as reporting and monitoring arrangements to ensure compliance with the said plan, as the same may be amended from time to time with the agreement of the Association, and “Resettlement Action Plans” or “RAPs” shall mean such Resettlement Action Plans, collectively.

“Resettlement Policy Framework” or “RPF” means the framework dated, March 2007, prepared by the Recipient and approved by the Association, for land acquisition or other associated Project impacts, resettlement and compensation under the Project, and in accordance with which Resettlement Action Plans shall be prepared and submitted to the Association for its approval, as the same may be amended from time to time with the concurrence of the Association.

“Service Contract” means a contract or contracts, as the case may be, to be financed by the Co-financiers, to be entered into between BWB, LWB and a private contractor or contractors, as the case may be, with requisite expertise in managing urban utilities, to assist BWB and LWB in improving their technical, operational and financial performance.
35. “Subproject” means a water and/or sanitation related activity proposed by local community(ies) in selected Market Centers and villages, for implementation by a RWB, financed or to be financed under Part B.2 of the Project, and “Subprojects” shall mean such Subprojects, collectively.

36. “Subproject Beneficiary” means a Market Center or village.

37. “Subsidiary Agreement” means the agreement referred to in paragraph A.1 and A.2 of Section II of Schedule 2 to this Agreement pursuant to which the Recipient shall make part of the proceeds of the Financing available to each Project Implementing Entity, and “Subsidiary Agreements” shall mean such Subsidiary Agreements, collectively.

38. “Water User Association” means a community-based group established by a District Assembly as a trust under the Trustee’s Incorporation Act, Chapter 5:03 of the laws of the Recipient, or as a cooperative under the Cooperative Societies Act, Chapter 47:02 of the laws of the Recipient, and to which the responsibility for managing a Market Center or rural piped water supply system is delegated.