Financing Agreement

(Third Programmatic Support for Institution Building Development Policy Financing)

between

ISLAMIC REPUBLIC OF AFGHANISTAN

and

INTERNATIONAL DEVELOPMENT ASSOCIATION

Dated June 17, 2007
GRANT NUMBER H295-AF

FINANCING AGREEMENT

AGREEMENT dated June 17, 2007, entered into between the ISLAMIC REPUBLIC OF AFGHANISTAN (“Recipient”) and INTERNATIONAL DEVELOPMENT ASSOCIATION (“Association”) for the purpose of providing financing in support of the Program (as defined in the Appendix to this Agreement). The Association has decided to provide this financing on the basis, inter alia, of: (a) the actions which the Recipient has already taken under the Program and which are described in Section I.1 of Schedule 1 to this Agreement; and (b) the Recipient’s maintenance of an appropriate macro-economic policy framework. The Recipient and the Association therefore hereby agree as follows:

ARTICLE I — GENERAL CONDITIONS; DEFINITIONS

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

1.02. Unless the context requires otherwise, the capitalized terms used in 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 in an amount equivalent to fifty two million nine hundred thousand Special Drawing Rights (SDR 52,900,000) (“Financing”).

2.02. The Recipient may withdraw the proceeds of the Financing in support of the Program in accordance with Section II of Schedule 1 to this Agreement.

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

2.04. The Payment Dates are February 15 and August 15 in each year.

2.05. The Payment Currency is Dollar.
ARTICLE III — PROGRAM

3.01 The Recipient declares its commitment to the Program and its implementation. To this end:

(a) the Recipient and the Association shall from time to time, at the request of either party, exchange views on the progress achieved in carrying out the Program;

(b) prior to each such exchange of views, the Recipient shall furnish to the Association for its review and comment a report on the progress achieved in carrying out the Program, in such detail as the Association shall reasonably request; and

(c) without limitation upon the provisions of paragraphs (a) and (b) of this Section, the Recipient shall exchange views with the Association on any proposed action to be taken after the disbursement of the Financing which would have the effect of materially reversing the objectives of the Program, or any action taken under the Program including any action specified in Section I of Schedule 1 to this Agreement.

ARTICLE IV — REMEDIES OF THE ASSOCIATION

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

ARTICLE V — EFFECTIVENESS; TERMINATION

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

ARTICLE VI — REPRESENTATIVE; ADDRESSES

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

6.02. The Recipient’s Address is:

Ministry of Finance
Kabul
Islamic Republic of Afghanistan
6.03. The Association’s Address is:

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

    Cable address:    Telex:    Facsimile:

    INDEVAS          248423(MCI)    1-202-477-6391
    Washington, D.C.

AGREED at Kabul, Islamic Republic of Afghanistan, as of the day and year first
above written.

    ISLAMIC REPUBLIC OF AFGHANISTAN

    By    /s/ Anwar-ul Haq Ahady
           Authorized Representative

    INTERNATIONAL DEVELOPMENT ASSOCIATION

    By    /s/ Alastair J. McKechnie
           Authorized Representative
SCHEDULE 1

Program Actions; Availability of Financing Proceeds

Section I. Actions Taken Under the Program

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

1. The Recipient’s cabinet has approved the budget for FY 1386 with due regard to sustainability in accordance with the Recipient’s medium-term fiscal framework.

2. The Recipient has, as part of its public administration reform program: (i) approved through the PAR Steering Committee, a plan for implementing the Civil Service Reform along with the cost estimates therefor; (ii) recruited more than one thousand four hundred (1,400) senior civil servants through merit-based recruitment procedures; (iii) approved through PAR Steering Committee, an action plan for the improvement of the merit-based selection process used by the Civil Service Appointments Board; and (iv) made individualized salary payments to more than eighty thousand (80,000) civil servants.

3. The Recipient has, as part of its public financial management reform program: (i) decreased the ARTF Ineligibility Ratio for Non-Wage Recurrent Expenditures to less than 0.26 for FY 1384; (ii) approved and adopted Ancillary Regulation to the Public Finance and Expenditure Management Law and the Procurement Law; and (iii) submitted to Parliament an audit report on the State Budget Accounts for FY 1385.

4. The Recipient’s cabinet has prepared and adopted a policy to restructure state-owned enterprises.

5. The Recipient has: (i) submitted to Parliament for enactment a draft Corporations Law and a draft Partnership Law; and (ii) published in its official gazette the amendments to the Insurance Law.

6. The Recipient’s cabinet has approved and implemented revised electricity tariff rates for the city of Kabul.

Section II. Availability of Financing Proceeds

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

B. Allocation of Financing Amounts. The Financing shall be withdrawn in a single tranche.
C. **Deposits of Financing Amounts.** Except as the Association may otherwise agree:

1. the Recipient shall open, prior to furnishing to the Association the first request for withdrawal from the Financing Account, and thereafter maintain the following two deposit accounts (“Deposit Accounts”) on terms and conditions satisfactory to the Bank:

   (a) a deposit account in Dollar (“Foreign Currency Deposit Account”); and

   (b) a deposit account in Afghani (“Local Currency Deposit Account”).

2. all withdrawals from the Financing Account shall be deposited by the Association into the Foreign Currency Deposit Account. Upon each deposit of an amount of the Financing into the Foreign Currency Deposit Account, the Recipient shall deposit an equivalent amount into the Local Currency Deposit Account.

D. **Audit.** Upon the Association’s request, the Recipient shall:

1. have the Deposit Accounts audited by independent auditors acceptable to the Association, in accordance with consistently applied auditing standards acceptable to the Association;

2. furnish to the Association as soon as available, but in any case not later than six (6) months after the date of the Association’s request for such audit, a certified copy of the report of such audit, of such scope and in such detail as the Association shall reasonably request; and

3. furnish to the Association such other information concerning the Deposit Accounts and their audit as the Association shall reasonably request.

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

F. **Closing Date.** The Closing Date is March 21, 2008.
APPENDIX

Section I. Definitions

1. “Afghani” means the currency of the Recipient.

2. “Ancillary Regulation” means, in respect of:
   (a) the Public Finance and Expenditure Management Law: the public finance regulation published in the Official Gazette 893, dated July 27, 2006; and
   (b) the Procurement Law: Procurement Rules of Procedures, dated April 12, 2007, issued by the Minister of Finance pursuant to Circular PPU/C005/1386.

3. “ARTF” means the Afghanistan Reconstruction Trust Fund established in March 2002, to support the Recipient’s recurrent and capital costs and to finance priority reconstruction projects and programs, which is administered by the Association and jointly managed by the Association, the United Nations Development Programme, the Asian Development Bank and the Islamic Development Bank.

4. “ARTF Ineligibility Ratio for Non-Wage Recurrent Expenditures” means the ratio of: (a) non-wage recurrent expenditures ineligible for ARTF financing, to (b) non-recurrent expenditures submitted to the ARTF Monitoring Agent.

5. “ARTF Monitoring Agent” means the independent firm contracted by the Association as administrator of ARTF, to monitor the procurement of goods and services, review and recommend approval of withdrawal applications and monitor all expenditures financed by ARTF grant funds.

6. “Civil Service Appointments Board” means the board established by the Recipient pursuant to Chapter 4 of the Civil Service Law (Law No. 862), dated September 22, 2005, for purposes of managing the appointment of senior civil servants.


8. “Civil Service Reform” means the Recipient’s administrative reform plan for FY1386 though 1390 aimed at increasing the efficiency of its civil service, as approved by PAR Steering Committee on April 2, 2007.
9. “Corporations Law” means the Recipient’s draft law intended to regulate the establishment and administration of corporations in the territory of the Recipient, as approved by presidential Decree No. 99 and filed with the Parliament by Letter 4042.


11. “Excluded Expenditure” means any expenditure:

(a) for goods or services supplied under a contract which any national or international financing institution or agency other than the Association or the Bank has financed or agreed to finance, or which the Association or the Bank has financed or agreed to finance under another credit, grant or loan;

(b) for goods included in the following groups or sub-groups of the Standard International Trade Classification, Revision 3 (SITC, Rev.3), published by the United Nations in Statistical Papers, Series M, No. 34/Rev.3 (1986) (the SITC), or any successor groups or subgroups under future revisions to the SITC, as designated by the Association by notice to the Recipient:

<table>
<thead>
<tr>
<th>Group</th>
<th>Sub-group</th>
<th>Description of Item</th>
</tr>
</thead>
<tbody>
<tr>
<td>112</td>
<td></td>
<td>Alcoholic beverages</td>
</tr>
<tr>
<td>121</td>
<td></td>
<td>Tobacco, un-manufactured, tobacco refuse</td>
</tr>
<tr>
<td>122</td>
<td></td>
<td>Tobacco, manufactured (whether or not containing tobacco substitutes)</td>
</tr>
<tr>
<td>525</td>
<td></td>
<td>Radioactive and associated materials</td>
</tr>
<tr>
<td>667</td>
<td></td>
<td>Pearls, precious and semiprecious stones, unworked or worked</td>
</tr>
<tr>
<td>718</td>
<td>718.7</td>
<td>Nuclear reactors, and parts thereof; fuel elements (cartridges), non-irradiated, for nuclear reactors</td>
</tr>
<tr>
<td>728</td>
<td>728.43</td>
<td>Tobacco processing machinery</td>
</tr>
<tr>
<td>897</td>
<td>897.3</td>
<td>Jewelry of gold, silver or platinum group metals (except watches and watch cases) and goldsmiths’ or silversmiths’ wares (including set gems)</td>
</tr>
<tr>
<td>971</td>
<td></td>
<td>Gold, non-monetary (excluding gold ores and concentrates)</td>
</tr>
</tbody>
</table>
(c) for goods intended for a military or paramilitary purpose or for luxury consumption;

(d) for environmentally hazardous goods, the manufacture, use or import of which is prohibited under the laws of the Recipient or international agreements to which the Recipient is a party;

(e) on account of any payment prohibited by a decision of the United Nations Security Council taken under Chapter VII of the Charter of the United Nations; and

(f) with respect to which the Association determines that corrupt, fraudulent, collusive or coercive practices were engaged in by representatives of the Recipient or other recipient of the Financing proceeds, without the Recipient (or other such recipient) having taken timely and appropriate action satisfactory to the Association to address such practices when they occur.

12. “Foreign Currency Deposit Account” means the account referred to in Part C.1(a) of Section II of Schedule 1 to this Agreement

13. “FY” means the Recipient’s fiscal year, commencing on March 21 of each calendar year and ending on March 20 of the following calendar year.

14. “General Conditions” means the “International Development Association General Conditions for Credits and Grants”, dated July 1, 2005 (as amended through October 15, 2006) with the modifications set forth in Section II of this Appendix.

15. “Independent Administration Reform and Civil Service Commission” means the Recipient’s reform commission established pursuant to Chapter 4 of the Civil Service Law.


17. “Local Currency Deposit Account” means the account referred to in Part C.1(b) of Section II of Schedule 1 to this Agreement.

18. “PAR Steering Committee” means the Recipient’s committee chaired by the Chairman of the Independent Administration Reform and Civil Service Commission, responsible for overseeing the Recipient’s public administration reforms.

20. “Partnership Law” means the Recipient’s draft law intended to regulate the establishment and administration of partnerships in the territory of the Recipient, as approved by presidential Decree No. 100 and filed with the Parliament by Letter 4042.


22. “Program” means the program of actions (other than those referred to security and the rule of law), objectives and policies designed to promote growth and achieve sustainable reductions in poverty and set forth or referred to in the letter dated April 2, 2007, from the Recipient to the Association declaring the Recipient’s commitment to the execution of the Program, and requesting assistance from the Association in support of the Program during its execution, such Program to exclude all aspects related to the promotion of security and rule of law.


24. “State Budget Accounts” means the financial annual statements as defined by Article 55 of the Public Finance and Expenditure and Management Law.

Section II. Modifications to the General Conditions

The modifications to the “International Development Association General Conditions for Credits and Grants”, dated July 1, 2005 (as amended through October 15, 2006) are as follows:

1. The last sentence of paragraph (a) of Section 2.03 (relating to Applications for Withdrawal) is deleted in its entirety.

2. Sections 2.04 (Designated Accounts) and 2.05 (Eligible Expenditures) are deleted in their entirety, and the remaining Sections in Article II are renumbered accordingly.

3. Sections 4.01 (Project Execution Generally), and 4.09 (Financial Management; Financial Statements; Audits) are deleted in their entirety, and the remaining Sections in Article IV are renumbered accordingly.

4. Paragraph (a) of Section 4.05 (renumbered as such pursuant to paragraph 3 above and relating to Use of Goods, Works and Services) is deleted in its entirety.

5. Paragraph (c) of Section 4.06 (renumbered as such pursuant to paragraph 3 above) is modified to read as follows:
“Section 4.06. Plans; Documents; Records

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

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

Section 4.07. Program Monitoring and Evaluation

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

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

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

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

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

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

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