Development Financing Agreement

(Poverty Reduction Support Project)

between

LAO PEOPLE’S DEMOCRATIC REPUBLIC

and

INTERNATIONAL DEVELOPMENT ASSOCIATION

Dated June 3, 2005
DEVELOPMENT FINANCING AGREEMENT

AGREEMENT, dated June 3, 2005, between LAO PEOPLE’S DEMOCRATIC REPUBLIC (the Borrower) and INTERNATIONAL DEVELOPMENT ASSOCIATION (the Association).

WHEREAS (A) the Association has received from the Borrower a letter dated March 4, 2005, describing a program of actions, objectives and policies designed to promote growth and achieve sustainable reductions in poverty (hereinafter called the Program), declaring the Borrower's commitment to the execution of the Program, and requesting assistance from the Association in support of the Program during the execution thereof;

(B) the Borrower has carried out the measures and taken the actions described in Schedule 2 of this Agreement to the satisfaction of the Association and has maintained a macroeconomic policy framework satisfactory to the Association; and

(C) on the basis, inter alia, of the foregoing, the Association has decided in support of the Program to provide such assistance to the Borrower by extending the Credit and the Grant as hereinafter provided;

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), with the modifications set forth below (the General Conditions), constitute an integral part of this Agreement:

(a) Section 1.01 is modified to read as follows:

“Section 1.01. Application of General Conditions

These General Conditions set forth the terms and conditions generally applicable to the Development Financing Agreement to the extent and subject to any modifications set forth in such agreement.”
(b) Section 2.01 is modified as follows:

(i) Paragraph 3 of Section 2.01 is modified to read as follows:

"3. “Borrower” means the party to the Development Financing Agreement to which the Financing is made.”

(ii) Paragraph 8 of Section 2.01 is modified to read as follows:

"8. “Development Financing Agreement” means the particular Development Financing Agreement to which these General Conditions apply, as such agreement may be amended from time to time. Development Financing Agreement includes these General Conditions as applied thereto, and all schedules and agreements supplemental to the Development Financing Agreement.”

(iii) The following new paragraphs are added after paragraph 11 of Section 2.01, and paragraphs 12 through 14 are renumbered as paragraphs 16 through 18 accordingly:

"12. “Grant” means the development grant provided for in the Development Financing Agreement.”

"13. “Grant Account” means the account opened by the Association on its books in the name of the Borrower to which the amount of the Grant is credited.”

"14. “Financing” means, collectively, the Credit and the Grant.”

"15. “Financing Accounts” means, collectively, the Credit Account and the Grant Account (or, where the context so requires, either of the Credit Account or the Grant Account).”

(iv) Section 2.01, paragraph 12, which is now re-numbered as paragraph 16, is modified to read as follows:

"16. “Project” means the program, referred to in the Preamble to the Development Financing Agreement, in support of which the Credit and the Grant are extended.”;

(c) The term “Credit”, wherever used in the following Articles and Sections of the General Conditions, is modified to read “Financing”: Sections 2.01(3), 2.01(12), 4.01, Article V, Article VI (excluding Section 6.05), Section 7.01(d), Article VIII, and Article IX.
The term “Credit Account”, wherever used in the following Articles and Sections of the General Conditions, is modified to read “Financing Accounts”: Section 2.01(6), the heading of Article III, 4.01, Article V, Article VI, and Section 12.03.

The term “Development Credit Agreement”, wherever used in the General Conditions, is modified to read “Development Financing Agreement”.

Article III is modified as follows:

(i) Section 3.01 is modified to read as follows:

“Section 3.01. **Financing Accounts**

The amount of the Credit shall be credited to the Credit Account and may be withdrawn from the Credit Account by the Borrower as provided in the Development Financing Agreement and in these General Conditions. The amount of the Grant shall be credited to the Grant Account and may be withdrawn from the Grant Account by the Borrower as provided in the Development Financing Agreement and in these General Conditions.”

(ii) The words “The principal of, and service charges on, the Credit” in Section 3.05 are modified to read “All amounts required to be paid under the Development Financing Agreement”.

Article IV is modified as follows:

(i) Section 4.01 is modified to read as follows:

“Section 4.01. **Currencies in which Withdrawals are to be made**.

Except as the Borrower and the Association shall otherwise agree, withdrawals from the Financing Accounts shall be made in the currency specified in Section 2.02(b) of the Development Financing Agreement; provided, however, that withdrawals in the currency of the Borrower shall be made in such currency or currencies as the Association shall from time to time reasonably select.”

(ii) Section 4.02(a) and the heading of Section 4.02 are modified to read as follows:

“Section 4.02. **Currencies in which Payments are to be Made**

(a) The Borrower shall pay all amounts required to be paid by it under the Development Financing Agreement in the
currency specified in such agreement or in such other eligible currency or currencies as may from time to time be designated or selected pursuant to paragraph (c) or (e) of this Section.”

(b) Wherever used in Section 4.02(c) and (e) of the General Conditions, the words “principal and service charges” are modified to read “amounts”.

(iii) Section 4.06 (b) is modified to read as follows:

“(b) All amounts which the Borrower shall be required to pay under the Development Financing Agreement shall be paid without restrictions of any kind imposed by, or in the territory of, the Borrower.”

(h) Article V is modified as follows:

(i) Section 5.01 is modified to read as follows:

“Section 5.01. Withdrawal from the Financing Accounts.

The Borrower shall be entitled to withdraw the proceeds of the Financing from the Financing Accounts in accordance with the provisions of the Development Financing Agreement and of these General Conditions.”

(ii) The last sentence of Section 5.03 is deleted.

(i) Article VI is modified as follows:

(i) The word “credit” in paragraphs (a)(ii) and (c)(i) of Section 6.02 is replaced with the words “credit, grant or financing”.

(ii) Section 6.03(c) is modified by replacing the words “corrupt or fraudulent” with the words “corrupt, fraudulent, collusive or coercive”.

(iii) Section 6.05 is modified to read as follows:

“Except as the Borrower and the Association shall otherwise agree, any cancellation of any amount of the Credit shall be applied pro rata to the several installments of the principal amount of the Credit maturing after the date of such cancellation.”
(j) Section 7.01 is modified to read as follows:

(i) The words “principal or interest or any other amount” in paragraph (b) are modified to read “any amount”.

(ii) The word “credit” in paragraph (b)(i) is replaced with the words “credit, grant or financing”.

(k) Section 8.01(a) is modified to read as follows:

“(a) All amounts which the Borrower shall be required to pay under the Development Financing Agreement shall be paid without deduction for, and free from, any taxes levied by, or in the territory of, the Borrower.”

(l) Section 9.04 is deleted in its entirety and Sections 9.05, 9.06 (as modified above), 9.07 and 9.08 are renumbered, respectively, Sections 9.04, 9.05, 9.06 and 9.07.

(m) Section 9.06 (c), now renumbered as 9.05 (c), is modified to read as follows:

“(c) Not later than six months after the Closing Date or such later date as may be agreed for this purpose between the Borrower and the Association, the Borrower shall prepare and furnish to the Association a report, of such scope and in such detail as the Association shall reasonably request, on the execution of the program referred to in the Preamble to the Development Financing Agreement, the performance by the Borrower and the Association of their respective obligations under the Development Financing Agreement and the accomplishment of the purposes of the Financing.”

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 meaning:

(a) “Bank of Lao PDR” means the Borrower’s Central Bank, and any successor thereto.

(b) “BCEL” means Banque pour Le Commerce Exterieur Lao, a wholly state-owned bank established and operating pursuant to the Decision of the President of the State bank of Lao PDR No. 129, dated November 1, 1989, and any successor thereto.

(c) “BP KP” means Bolisat Pattana Khet Pudo, a wholly state-owned enterprise established and operating pursuant to Decree No. 188, dated August 19, 1984, and any successor thereto.
(d) “Deposit Account” means the account referred to in Section 2.02(b) of this Agreement.

(e) “FY” means the Borrower’s fiscal year extending from October 1 through September 30 of each calendar year.

(f) “IAS” means international auditing standards.

(g) “Lao Airlines” means the wholly state-owned enterprise established and operating pursuant to Decision No. 771/MCTPC dated May 23, 1989 of the Borrower’s Ministry of Communication, Transport, Post and Construction, and any successor thereto.

(h) “LDB” means Lao Development Bank, a wholly state-owned bank, established pursuant to the merger of Lane Xang Bank and Lao May Bank in 2004, and any successor thereto.

(i) “NPL” means Nam Papa Laos, a wholly state-owned enterprise established and operating pursuant to Decision No. 1296, dated April 5, 2001, of the Borrower’s Ministry of Transport and Communications, and any successor thereto.

(j) “PEMSP” and “Public Expenditure Management Strengthening Program” mean a program of actions, supported by technical assistance, designed to improve policy consistency, efficiency, transparency and accountability in the Borrower’s management of public expenditures.

(k) “PH3” means Pharmaceutical Factory 3, a wholly state-owned enterprise established and operating pursuant to Resolution No. 275, dated May 15, 1987, of the Borrower’s Ministry of Health, and any successor thereto.

(l) “PrMO” and “Procurement Monitoring Office” mean the office within the Borrower’s Ministry of Finance established and operating pursuant to the Prime Minister’s Decree No. 03/PM dated January 9, 2004 on Government Procurement of Goods, Works, Maintenance and Services, and the Minister of Finance’s Decision No. 2382/MOF dated November 4, 2004, for purposes of monitoring the procurement activities of all government agencies and ensuring their compliance with the Implementing Rules and Regulations of said Decree.
ARTICLE II

The Financing

Section 2.01. The Association agrees to make available to the Borrower, on the terms and conditions set forth or referred to in this Agreement:

(a) an amount in various currencies equivalent to three million Special Drawing Rights (SDR3,000,000) (the Credit); and

(b) an amount in various currencies equivalent to three million six hundred thousand Special Drawing Rights (SDR3,600,000) (the Grant).

Section 2.02. (a) Subject to the provisions of paragraphs (b), (c) and (d) of this Section, the Borrower shall be entitled to withdraw the amount of the Credit from the Credit Account and the amount of the Grant from the Grant account in support of the Program.

(b) Except as the Association may otherwise agree: (i) all withdrawals from the Financing Accounts shall be deposited by the Association into an account in United States Dollars designated by the Borrower and acceptable to the Association; and (ii) the Borrower shall ensure that upon each deposit of an amount of the Credit or of the Grant into said account, an equivalent amount is accounted for in the Borrower’s budget management system, in a manner acceptable to the Association.

(c) The Borrower undertakes that the proceeds of the Financing shall not be used to finance expenditures excluded pursuant to the provisions of Schedule 1 to this Agreement. If the Association determines at any time that an amount of the Financing was used to make a payment for an expenditure so excluded, the Borrower shall promptly upon notice from the Association, refund an amount equal to the amount of said payment to the Association. Amounts refunded to the Association upon such request shall be cancelled.

Section 2.03. The Closing Date shall be December 31, 2005, 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: (i) 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, such rate not to exceed the rate of one-half of one percent (1/2 of 1%) per annum; and (ii) a commitment charge on the principal amount of the Grant not withdrawn from time to time at a rate to be set by the Association as of June 30 of each year, such rate not to exceed the rate of one-half of one percent (1/2 of 1%) per annum.
(b) Each 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 the Grant Account (as the case may be), or canceled; and (ii) at the respective 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 respective 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) Each 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 March 15 and September 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 March 15 and September 15, commencing September 15, 2015 and ending March 15, 2045. Each installment to and including the installment payable on March 15, 2025 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 the Association 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

Particular Covenants

Section 3.01. (a) The Borrower 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 Borrower 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.

(c) Without limitation upon the provisions of paragraph (a) of this Section, the Borrower 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 Schedule 2 to this Agreement.

Section 3.02. (a) Without limitation upon the provisions of Section 9.01(a) of the General Conditions, the Borrower shall promptly furnish to the Association such information relating to the provisions of Article II of this Agreement as the Association may, from time to time, reasonably request.
Upon the Association’s request, the Borrower shall:

(i) have the Deposit Account audited by independent auditors acceptable to the Association, in accordance with consistently applied auditing standards and under terms of reference acceptable to the Association;

(ii) furnish to the Association as soon as available, but in any case not later than four months after the date of the Association’s request for such audit, a certified copy of the report of such audit by said auditors, of such scope and in such detail as the Association shall have reasonably requested; and

(iii) furnish to the Association such other information concerning the Deposit Account and the audit thereof as the Association shall have reasonably requested.

ARTICLE IV

Additional Event of Suspension

Section 4.01. Pursuant to Section 6.02 (l) of the General Conditions, the following additional event is specified, namely, that a situation has arisen which shall make it improbable that the Program, or a significant part thereof, will be carried out.

ARTICLE V

Effective Date; Termination

Section 5.01. The following event is specified as an additional condition to the effectiveness of the Development Financing Agreement within the meaning of Section 12.01 (b) of the General Conditions, namely, that the Development Grant Agreement for the Nam Theun 2 Hydroelectric Power Project has become effective.

Section 5.02. The date ninety (90) days after the date of this Agreement is hereby specified for the purposes of Section 12.04 of the General Conditions.
ARTICLE VI

Representative of the Borrower; Addresses

Section 6.01. The Minister of Finance of the Borrower is designated as the representative of the Borrower for the purposes of Section 11.03 of the General Conditions.

Section 6.02. The following addresses are specified for the purposes of Section 11.01 of the General Conditions:

For the Borrower:

Ministry of Finance
Post Box No.46
Vientiane
Lao PDR

Facsimile: 856-21-911370

For the Association:

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

Cable address: INDEVAS
Telex: 248423 (MCI) or 64145 (MCI)
Facsimile: (1-202) 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 Vientiane, Lao People’s Democratic Republic, as of the day and year first above written.

LAO PEOPLE’S DEMOCRATIC REPUBLIC

By /s/ Somdy Douangdy

Authorized Representative

INTERNATIONAL DEVELOPMENT ASSOCIATION

By /s/ Ian Porter

Authorized Representative
SCHEDULE 1

Excluded Expenditures

For purposes of Section 2.02(c) of this Agreement, the proceeds of the Financing shall not be used to finance any of the following expenditures:

1. expenditures for goods or services supplied under a contract which any national or international financing institution or agency other than the Bank or the Association shall have financed or agreed to finance, or which the Association or the Bank shall have financed or agreed to finance under another credit, loan or grant;

2. expenditures for goods included in the following groups or subgroups 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 Borrower:

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<th>Subgroup</th>
<th>Description of Items</th>
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<td>971</td>
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<td>Gold, non-monetary (excluding gold ores and concentrates)</td>
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3. expenditures for goods intended for a military or paramilitary purpose or for luxury consumption;

4. expenditures for environmentally hazardous goods (for purposes of this paragraph the term “environmentally hazardous goods” means goods, the manufacture, use or import of which is prohibited under the laws of the Borrower or international agreements to which the Borrower is a party;

5. expenditures on account of any payment to persons or entities, or any import of goods, if such payment or import is prohibited by a decision of the United Nations Security Council taken under Chapter VII of the Charter of the United Nations; and

6. expenditures under a contract in respect of which the Association determines that corrupt, fraudulent, collusive or coercive practices were engaged in by representatives of the Borrower or of a beneficiary of the Financing during the procurement or execution of such contract, without the Borrower having taken timely and appropriate action satisfactory to the Association to remedy the situation.
SCHEDULE 2

Actions Referred to in Recital (B) of the Preamble to this Agreement

Public Expenditure Management

1. The Borrower’s Ministry of Finance has approved a Public Expenditure Management Strengthening Program together with an annual implementation plan therefor for Fiscal Year 2004-2005, acceptable to the Association.

2. The Borrower’s Ministry of Finance has provided to the Association a summary of the final budget for Fiscal Year 2004-2005, acceptable to the Association.

3. The Borrower’s Treasury has updated the registers of: (a) accounts payable, by period, as at end of Fiscal Year 2003-2004; and (ii) government bank accounts, with their respective balances as at end of Fiscal Year 2003-2004.

4. The Borrower’s Ministry of Finance has approved the Charter of the Procurement Monitoring Office.

The Banking Sector

5. Bank of Lao People’s Democratic Republic has provided to the Ministry of Finance the independent IAS audit reports of the 2003 accounts of BCEL and LDB.

Performance of State-owned Enterprises

6. The FY03 state audits of Lao Airlines, NPL and PH3 have been completed

7. Re-structuring of Lao Airlines and of BPKP is proceeding in accordance with the provisions of the re-structuring plan set forth in the Notice No. 059/CPMO dated 29 April 2004 issued by the Prime Minister’s Office.

Spending for Pro-poor NGPES Priorities

8. The Borrower’s Ministry of Health has paid the salaries of health care workers through the period ending on January 31, 2005 such that, as of that date, no more than 20% of health care worker salaries remaining due have been outstanding more than 2 months.

9. The Borrower’s Ministry of Education has paid the salaries of teachers through the period ending on January 31, 2005 such that, as of that date, no more than 20% of teacher salaries remaining due have been outstanding more than 2 months.
Private Sector Development

10. The National Assembly has enacted the Revised Domestic and Foreign Investment Laws.