
GRANT NUMBER 0139-TUV(SF)

GRANT AGREEMENT
(Special Operations)
(Improved Financial Management Program)

between

TUVALU

and

ASIAN DEVELOPMENT BANK

DATED 03 FEBRUARY 2009

GAS: TUV 41180

**GRANT AGREEMENT
(Special Operations)**

GRANT AGREEMENT dated 03 February 2009 between TUVALU (hereinafter called the Recipient) and ASIAN DEVELOPMENT BANK (hereinafter called ADB).

WHEREAS

(A) ADB has received from the Recipient a development policy letter dated 11 November 2008 (hereinafter called the Policy Letter), setting forth certain objectives, policies and actions, described in Schedule 1 to this Grant Agreement, designed to strengthen the Recipient's public financial management (hereinafter called the Program);

(B) the Recipient has applied to ADB for a grant for the purposes of the Program; and

(C) ADB has agreed to provide a grant to the Recipient from ADB's Special Funds resources upon the terms and conditions hereinafter set forth;

NOW THEREFORE the parties agree as follows:

ARTICLE I

Grant Regulations; Definitions

Section 1.01. All provisions of the Special Operations Grant Regulations of ADB, dated 7 February 2005 (hereinafter called the Grant Regulations), are hereby made applicable to this Grant Agreement with the same force and effect as if they were fully set forth herein, subject, however, to the following modifications:

(a) Section 2.01(15) is deleted and the following is substituted therefore:

24. The term "Program" means the program for which ADB has agreed to make the Grant, as described in the Grant Agreement and as such description may be amended from time to time by agreement between ADB and the Recipient.

(b) The term "Project" wherever it appears in the Grant Regulations shall be substituted by the term "Program".

(c) Section 2.01(17) is deleted the following is substituted therefore:

17. The term "Program Executing Agency" means the entity or entities responsible for the carrying out of the Program as specified in the Grant Agreement.

(d) The term "Project Executing Agency" wherever it appears in the Grant Regulations shall be substituted by the term "Program Executing Agency".

(e) Section 5.01(a) is deleted and the following is substituted therefore:

(a) Subject to any conditions or restrictions specified in the Grant Agreement, the Recipient shall be entitled to withdraw from the Grant Account such amounts as shall be required to meet payments for expenditures required for the Program and to be financed under the Grant Agreement.

Section 1.02. The definitions set forth in the Grant Regulations are applicable to this Grant Agreement unless the context requires otherwise. In addition, the following terms have the following meanings:

(a) "Counterpart Funds" means the Australian dollar proceeds accruing to the Recipient and generated from the Grant proceeds under the Program;

(b) "Deposit Account" means the account referred to in Paragraph 4(a) of Schedule 2 to this Grant Agreement;

(c) "Eligible Items" means the goods imported under the Program (except those specifically excluded pursuant to Attachment 1 to Schedule 2 to this Grant Agreement) and, services in connection with the delivery and installation of such goods and consulting services, the foreign exchange costs of which are eligible for financing out of the proceeds of the Grant;

(d) "First Tranche" means the portion of the proceeds of the Grant in an amount not exceeding an amount of \$1,240,000 to be initially withdrawn and utilized;

(e) "Government" means Cabinet of Ministers of the Recipient;

(f) "MFEP" means the Ministry of Finance and Economic Planning of the Recipient;

(g) "NBT" means the National Bank of the Recipient;

(h) "OIASA" means the Outer Island Agency Suspense Account;

(i) "OIASA Overdraft" means the government debt in the amount of A\$3,796,000 to NBT;

(j) "PFTAC" means the Pacific Financial Technical Assistance Centre;

(k) "Policy Matrix" means the policy matrix as agreed between the Recipient and ADB and attached to the Policy Letter;

(l) "PSC" means the program steering committee as described in Paragraph 2 of Schedule 4 to this Grant Agreement; and

(m) "Second Tranche" means the portion of the proceeds of the Grant in an amount not exceeding \$2,000,000, to be withdrawn, at any time after the withdrawal of the First Tranche, pursuant to and subject to the provisions of Paragraph 5 of Schedule 2 to this Grant Agreement.

ARTICLE II

The Grant

Section 2.01. ADB agrees to make available to the Recipient from ADB's Special Funds resources on terms and conditions set forth in this Agreement an amount of Three Million Two Hundred Forty Thousand Dollars (\$3,240,000).

ARTICLE III

Use of Proceeds of the Grant

Section 3.01. The Recipient shall cause the proceeds of the Grant to be applied to the financing of expenditures on the Program in accordance with the provisions of this Grant Agreement.

Section 3.02. The proceeds of the Grant may be withdrawn from the Grant Account only for the purposes of financing expenditures incurred for Eligible Items under the Program in accordance with the provisions of Schedule 2 to this Grant Agreement, as such Schedule may be amended from time to time by agreement between the Recipient and ADB.

Section 3.03. Except as ADB may otherwise agree, all ineligible Items to be financed out of the proceeds of the Grant shall be procured in accordance with the provisions of Schedule 3 to this Grant Agreement.

Section 3.04. Withdrawals from the Grant Account shall be made only on account of expenditures which:

- (a) are produced in, and supplied from, such member countries of ADB as shall have been specified by ADB from time to time as eligible sources for procurement, and

- (b) meet such other eligibility requirements as shall have been specified by ADB from time to time.

Section 3.05. The Grant Closing Date for the purposes of Section 8.02 of the Grant Regulations shall be 30 September 2010 or such other date as may from time to time be agreed between the Recipient and ADB.

ARTICLE IV

Particular Covenants

Section 4.01. In the carrying out of the Project and operation of the Project facilities, the Recipient shall perform, or cause to be performed, all obligations set forth in Schedule 4 to this Grant Agreement.

Section 4.02. (a) The Recipient shall maintain, or cause to be maintained, records and documents adequate to identify the Eligible Items financed out of the proceeds of the Grant and to record the progress of the Program.

(b) The Recipient shall enable ADB's representatives to inspect any relevant records and documents referred to in paragraph (a) of this section.

Section 4.03 (a) As part of the reports and information referred to in Section 6.04 of the Grant Regulations, the Recipient shall furnish, or cause to be furnished, to ADB all such reports and information as ADB shall reasonably request concerning the implementation of the Program, including the accomplishment of the targets and carrying out of the actions set out in the Policy Letter.

(b) Without limiting the generality of the foregoing or Section 6.04 of the Grant Regulations, the Recipient shall furnish, or cause to be furnished, to ADB semi-annual reports on the carrying out of the Program and on the accomplishment of the targets and carrying out of the actions set out in the Policy Letter.

ARTICLE V

Effectiveness

Section 5.01. The following is specified as an additional condition to the effectiveness of this Grant Agreement for the purposes of Section 9.01(e) of the Grant Regulations: all conditions for the release of the First Tranche, specified in Attachment 2 to Schedule 2 to this Grant Agreement, shall have been met.

Section 5.02. A date ninety (90) days after the date of this Grant Agreement is specified for the effectiveness of the Grant Agreement for the purposes of Section 9.04 of the Grant Regulations.

ARTICLE VI

Miscellaneous

Section 6.01. The Minister of Finance and Economic Planning of the Recipient is designated as representative of the Recipient for the purposes of Section 11.02 of the Grant Regulations.

Section 6.02. The following addresses are specified for the purposes of Section 11.01 of the Grant Regulations:

For the Recipient

The Secretary
Ministry of Finance and Economic Planning
Private Bag
Funafuti, Tuvalu

Facsimile Number:

(688) 20210.

For ADB

Asian Development Bank
P.O. Box 789
0980 Manila, Philippines

Facsimile Numbers:

(632) 636-2444
(632) 636-2446.

IN WITNESS WHEREOF the parties hereto, acting through their representatives thereunto duly authorized, have caused this Grant Agreement to be signed in their respective names and to be delivered at the principal office of ADB, as of the day and year first above written.

TUVALU



By _____
 LOTOALA METIA
 Authorized Representative

ASIAN DEVELOPMENT BANK

By _____
 HARUHIKO KURODA
 President

SCHEDULE 1**Description of the Program**

1. The intended impact of the Program is sustained economic growth and fiscal stability through strengthening fiscal planning and management as prioritized in the national plan objectives of the Recipient. The expected outcome of the Program is improved fiscal planning and management capacity.
2. The Program is described in more detail in the Policy Letter. The Program is expected to be implemented by 31 March 2010.
3. In support of the Program:
 - (a) the proceeds of the Grant shall be used to finance the foreign exchange costs of Eligible Items; and
 - (b) the Counterpart Funds shall be used to finance the local currency costs relating to the implementation of certain programs and activities consistent with the objectives of the Program, pursuant to the provisions of Paragraph 7 of Schedule 4 to this Grant Agreement.
4. The proceeds of the Grant are expected to be utilized by 30 September 2010.

SCHEDULE 2**Allocation and Withdrawal of Grant Proceeds**

1. Except as ADB may otherwise agree, the following provisions of this Schedule shall apply to the withdrawal of Grant proceeds from the Grant Account.

2. (a) Withdrawals from the Grant Account shall be made for the financing of the cost of Eligible Items.

(b) No withdrawals from the Grant Account shall be made in respect of any expenditures which have been financed by credits from official international or bilateral aid agencies or any other loan or grant made by ADB.

3. (a) An application for withdrawal from the Grant Account shall be submitted to ADB by the Recipient and shall be in a form satisfactory to ADB.

(b) Such withdrawal applications shall be accompanied by a certificate of the Recipient confirming that with respect to each year during which the proceeds of the Grant are expected to be disbursed, the value of the Eligible Imports is expected to be equal to or greater than the amount of the Grant expected to be disbursed during such year.

(c) For the purposes of this paragraph, the term "Eligible Imports" means the total imports of the Recipient during the relevant period minus the following imports during the same period:

- (i) imports from countries which are not members of ADB;
- (ii) imports for ineligible items specified in the Attachment to this Schedule; and
- (iii) imports financed from credits from official international or bilateral aid agencies or any other loan or grant made by ADB.

(d) The Recipient shall allow experts appointed by ADB to verify the value of Eligible Imports during any period in respect of which the Recipient has certified the value of Eligible Imports in its withdrawal application.

4. (a) Prior to submitting the first application to ADB for withdrawal from the Grant Account, the Recipient shall nominate an account ("Deposit Account") at NBT into which all withdrawals from the Grant Account shall be deposited. The Deposit Account shall be established, managed and liquidated in accordance with terms and conditions satisfactory to ADB.

(b) Separate accounts and records in respect of the Deposit Account shall be maintained in accordance with consistently maintained sound accounting principles. Upon ADB's request, the Recipient shall have the Deposit Account audited by independent auditors, whose qualifications, experience and terms of reference are acceptable to ADB, in accordance with appropriate auditing standards. Promptly after their preparation but in any event not later than six (6) months after the date of ADB's request, certified copies of such audited accounts and records shall be furnished to ADB, all in the English language.

(c) Throughout the Program implementation period, the Recipient shall submit trade statistics and any other information as ADB may require from time to time to assess the Recipient's compliance with the formula for determining Eligible Imports.

5. Notwithstanding any other provision of this Grant Agreement or the Grant Regulations and except as ADB may otherwise agree, no withdrawals shall be made from the Second Tranche unless ADB shall be satisfied, after consultation with the Recipient, that (i) sufficient progress has been achieved by the Recipient in the carrying out of the Program; and, in particular, (ii) the Recipient has fulfilled the conditions for the release of the Second Tranche specified in Attachment 3 to this Schedule.

Negative List

1. Grant proceeds will finance the foreign currency expenditures for the reasonable cost of imported goods required during the Improved Financial Management Program.
2. No withdrawals will be made for the following:
 - (i) expenditures for goods included in the following groups or sub-groups of the United Nations Standard International Trade Classification, Revision 3 (SITC, Rev. 3) or any successor groups or sub-groups under future revisions to the SITC, as designated by ADB by notice to the Recipient:

Ineligible Items

Chapter	Heading	Description of Items
112		Alcoholic beverages
121		Tobacco, unmanufactured; tobacco refuse
122		Tobacco, manufactured (whether or not containing tobacco substitute)
525		Radioactive and associated materials
667		Pearls, precious and semiprecious stones, unworked or worked
718	718.7	Nuclear reactors, and parts thereof, fuel elements (cartridges), nonirradiated for nuclear reactors
728	728.43	Tobacco processing machinery
897	897.3	Jewelry of gold, silver or platinum-group metals (except watches and watch cases) and goldsmiths' or silversmiths' wares (including set gems)
971		Gold, nonmonetary (excluding gold ore and concentrates)

Source: United Nations.

- (ii) expenditures in the currency of the Recipient or of goods supplied from the territory of the Recipient;
- (iii) expenditures for goods supplied under a contract that any national or international financing institution or agency will have financed or has agreed to finance, including any contract financed under any loan or grant from the ADB;
- (iv) expenditures for goods intended for a military or paramilitary purpose or for luxury consumption;
- (v) expenditures for narcotics;
- (vi) expenditures 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; and

- (vii) expenditures on account of any payment prohibited by the Recipient in compliance with a decision of the United Nations Security Council taken under Chapter VII of the Charter of the United Nations.

Conditions for Release of the First Tranche

Improve Public Debt Management Capacity

1. The Parliament to pass taxation reform legislation (an Income Tax Act Amendment, a Customs Act Amendment and a Consumption Tax Bill).
2. The Government to approve the development of a Debt Risk Management and Mitigation Policy and Strategy, which shall include:
 - (a) the processes and responsibilities for the analysis and approval of proposed new guarantees and debt;
 - (b) processes for prioritizing and scheduling debt repayment including debt which is currently not being repaid; and
 - (c) a schedule of timely and standardized reporting on Government's debt portfolio.

Strengthen Oversight of Public Enterprises

3. The Government to approve the preparation of a Public Enterprise Governance Reform Strategic Policy, which shall include:
 - (a) government's service delivery priorities and requirements;
 - (b) identification of strategic assets and position on ownership of each enterprise;
 - (c) a process for review of the social and sustainability implications of changes in ownership of government assets; and
 - (d) identification of small government business-like activities for possible transfer to the private sector.

Strengthen Management Capacity in Public Enterprises

4. The Government to approve the preparation of a Public Corporations Act, which shall include:
 - (a) the roles of the board of directors and management of a public corporation, and procedures and criteria for their appointment and dismissal;
 - (b) the requirement for periodic disclosure of information and filing of audited accounts;

- (c) a procedure for decorporatization;
- (d) the roles of the relevant ministers and the Auditor General of the Recipient; and
- (e) a provision for the introduction of performance contracts for management.

5. MFEP to prepare a detailed review of private sector business potential covering the analysis of sector lending and loan repayment trends, collation of informal information through sources such as the Recipient's Chamber of Commerce, as well as identification of successful small businesses and a brief analysis of why they are successful.

Conditions for Release of the Second Tranche

1. The conditions to be fulfilled by the Recipient for the release of the Second Tranche are, maintaining the conditions satisfied under the First Tranche and achievement, satisfactory to ADB, of the conditions set out below.

Improve Public Debt Management Capacity

2. Government to approve the Debt Risk Management and Mitigation Policy and Strategy, which shall include:

- (a) processes and responsibilities for the analysis and approval of proposed new guarantees and debt;
- (b) processes for prioritizing and scheduling debt repayment including debt which is currently not being repaid; and
- (c) a schedule of timely and standardized reporting on Government's debt portfolio.

3. The Government to prepay part of the OIASA Overdraft using the counterpart funds generated from the proceeds of the First Tranche.

Strengthen Oversight of Public Enterprises

4. The Government to approve the Public Enterprise Governance Reform Strategic Policy, which shall include:

- (a) service delivery priorities and requirements;
- (b) identification of strategic assets and position on ownership of each enterprise;
- (c) a process for review of the social and sustainability implications of changes in ownership of government assets; and
- (d) identification of small government business-like activities for possible transfer to the private sector.

5. The Government to submit to the Parliament a draft Public Corporations Act, which shall include:

- (a) roles of the board of directors and management of a public corporation, and procedures and criteria for their appointment and dismissal;

- (b) requirements for periodic disclosure of information and filing of audited accounts;
- (c) a procedure for decorporatization; and
- (d) a provision for the introduction of performance contracts for management.

Strengthen Management Capacity in Public Enterprises

6. MFEP to undertake a detailed assessment of private sector potential, which shall reflect the results of community consultation. The assessment shall cover:

- (a) private sector capacity to undertake small scale management contracts;
- (b) additional upstream and downstream business potential as a result of management contracts as well as untapped business potential from existing businesses;
- (c) identification of new business niches;
- (d) assessment of business support requirements, including business and accounting services; and
- (e) assessment of Outer Island business opportunities.

7. NBT to adopt written and board-approved policies, as proposed in PFTAC report of July 2008, for:

- (a) the timely collection of past due loans and advances of credit; and
- (b) measuring, monitoring and maintaining adequate liquidity.

8. The Parliament to adopt a legal framework for the licensing and on-going supervision and regulation of banking institutions, which shall provide for implementation and adherence to the Basel Core Principles for Effective Banking Supervision.

SCHEDULE 3

Procurement

1. Except as ADB may otherwise agree, the procedures referred to in the following paragraph of this Schedule shall apply in the procurement of Eligible Items to be financed out of the proceeds of the Grant.

2. (a) Except as provided in Paragraph 2(b) below, each contract for Eligible Items shall be awarded on the basis of either the purchaser's normal commercial procurement practices, in the case of procurement by the private sector, or the Recipient's prescribed procurement procedures, in the case of procurement by the public sector, having due regard for the principles of economy and efficiency.

(b) Each supply contract for Eligible Items which are commonly traded commodities shall be awarded on the basis of procedures appropriate to the trade and acceptable to ADB.

SCHEDULE 4

Program Implementation; Counterpart Funds; Other Matters

Management and Coordination

1. MFEP shall be the Program Executing Agency, which is responsible for the coordination of policy, legal and regulatory actions and ensuring that all actions are carried out in a timely manner.
2. The Recipient shall establish, by 31 January 2009, a PSC to be chaired by Secretary of MFEP and to include representatives of the Office of the Attorney General of the Recipient, and MFEP's budget and public enterprise oversight areas to monitor and coordinate the Program and supporting technical assistance from ADB and other donors.

Implementation of the Policy Letter

3. The Recipient shall (a) ensure that the policies adopted and actions taken as described in the Policy Letter, including the Policy Matrix, prior to the date of this Grant Agreement continue in effect for the duration of the Program period and subsequently; and (b) promptly adopt all other policies and take all other actions indicated in the Policy Letter, including the Policy Matrix, and ensure that such policies and actions continue in effect for the duration of the Program period and subsequently.

Policy Dialogue

4. The Recipient shall keep ADB informed of, and the Recipient and ADB shall from time to time exchange views on, the progress made in carrying out the policies and actions set out in the Policy Letter and the Policy Matrix.
5. The Recipient shall continue timely policy dialogue with ADB on problems and constraints encountered during implementation of the Program and on desirable changes to overcome or mitigate such problems and constraints.
6. The Recipient shall keep ADB informed of policy discussions with other multilateral or bilateral aid agencies that have implications for implementation of the Program, and shall provide ADB with an opportunity to comment on any resulting policy proposals. The Recipient shall take ADB's views into consideration before finalizing and implementing any such proposals.

Counterpart Funds

7. Throughout the implementation of the Program, the Recipient shall ensure that adequate resources are allocated and released in a timely manner in order to ensure proper implementation of the Program as described in Paragraph 1 of Schedule 1 to this Grant Agreement and the Policy Letter. The Recipient shall ensure that the Counterpart Funds shall be used, first, to repayment of the OIASA Overdraft, and, second, towards outstanding debt of the Recipient to NBT.

Program Performance Monitoring and Evaluation

8. The Recipient shall cause MFEP to (a) establish, within three (3) months after the Effective Date, and maintain a program performance evaluation system, which shall include a data base on the status of policy measures and program indicators based on the Policy Matrix and the design and monitoring framework for the Program, (b) monitor the implementation of the Program and its impacts on budget outcomes and public enterprise performance, and (iii) submit to ADB semi-annual reports on the implementation of the Program, including accomplishment of the measures set forth in the Policy Letter and the Policy Matrix.

Anticorruption

9. The Recipient shall undertake necessary measures to create and sustain a corruption free environment, ensure that its anticorruption law and regulations and ADB's *Anticorruption Policy* (1998, as amended to date) are strictly enforced and complied with during the Program implementation, and facilitate ADB's exercising its right to investigate, directly or through its agents, any alleged corrupt, fraudulent, collusive or coercive practices relating to the Program.

Program Review

10. The Recipient, in consultation with ADB and PFTAC, shall jointly review the progress of the Program implementation. Based on these reviews, modifications and improvements will be considered. To facilitate such review, the Recipient shall assist ADB by providing relevant data and information in such detail as ADB may reasonably request.

11. Approximately six (6) weeks before the anticipated withdrawal of the Second Tranche, or such other time as the Recipient and ADB may agree, a review shall be carried out concerning the Recipient's progress in implementing the policy reforms under the Program set out in the Policy Letter and the Policy Matrix, including the fulfillment of the conditions listed in Attachment 3 to Schedule 2 to this Grant Agreement.