
LOAN NUMBER 2659-RMI (SF)

LOAN AGREEMENT
(Special Operations)

(Public Sector Program – Subprogram 1)

between

REPUBLIC OF THE MARSHALL ISLANDS

and

ASIAN DEVELOPMENT BANK

DATED 8 SEPTEMBER 2010

LPS:RMI 43321

LOAN AGREEMENT (Special Operations)

LOAN AGREEMENT dated 8 September 2010 between REPUBLIC OF THE MARSHALL ISLANDS (the "Borrower") and ASIAN DEVELOPMENT BANK ("ADB").

WHEREAS

(A) ADB has received from the Borrower a development policy letter dated 28 June 2010 (the "Policy Letter"), setting forth certain objectives, policies and actions, described in Schedule 1 to this Loan Agreement, designed to support the reform of the Borrower's public sector under a cluster of subprograms (the "Program Cluster") forming the Public Sector Program, some of which the Borrower has implemented as prior actions under the first subprogram of the Program Cluster ("Subprogram 1" or the "Program") as described in Schedule 1 to this Loan Agreement;

(B) the Borrower has applied to ADB for a loan from its Special Funds resources for the purposes of the Program;

(C) parts of the Program will be carried out by the Marshalls Energy Company ("MEC") upon the terms and conditions set forth in the Program Agreement as defined below; and

(D) ADB has, on the basis inter alia of the foregoing, agreed to make a loan to the Borrower from ADB's Special Funds resources upon the terms and conditions hereinafter set forth and in the Program Agreement.

NOW THEREFORE the parties agree as follows:

ARTICLE I

Loan Regulations; Definitions

Section 1.01. All the provisions of the Special Operations Loan Regulations of ADB, dated 1 January 2006 (the "Loan Regulations"), are hereby made applicable to this Loan 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(24) is deleted and the following is substituted therefor:

(24) The term "Program" means Subprogram 1 as referred to in Recital A for which ADB has agreed to make the Loan, as described in the Loan Agreement and as the description thereof may be amended from time to time by agreement between ADB and the Borrower.

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

(c) The term "Project Agreement" wherever it appears in the Loan Regulations shall be substituted by the term "Program Agreement."

(d) Sections 2.01 (25) is deleted and the following is substituted therefor:

(25) "Project Agreement" means the Program Agreement of even date herewith between ADB and MEC".

(e) Section 2.01(26) is deleted and the following is substituted therefor:

(26) The term "Program Executing Agency" means the entity or entities responsible for the carrying out of the Program as specified in the Loan Agreement. The term "Project Executing Agency" wherever it appears in the Loan Regulations shall be substituted by the term "Program Executing Agency".

(f) Section 6.05 (c) is deleted and the following is substituted therefor:

(c) Promptly after the closing date for withdrawals from the Loan Account, but in any event not later than 3 months thereafter or such later date as may be agreed for this purpose between the Borrower and ADB, the Borrower shall prepare and furnish to ADB a report, in such form and in such detail as ADB shall reasonably request, on the execution of the Program, including its cost, the performance by the Borrower of its obligations under this Loan Agreement and the accomplishment of the purposes of the Loan.

Section 1.02. The terms defined in the Loan Regulations are incorporated into this Loan Agreement, unless the context requires otherwise. In addition, the following terms have the following meanings:

(a) "CAP" means the Comprehensive Adjustment Program advisory group established by the MOF;

(b) "Combined Utilities Board" means the Marshalls Energy Company Board of Directors, established by the Borrower to oversee and regulate MEC and which may also from time to time oversee and regulate the operations of other utilities of the Borrower or any successor thereto acceptable to ADB;

(c) "Counterpart Funds" means the Dollar proceeds accruing to the Borrower and generated from the proceeds of the Loan, referred to in paragraph 5 of Schedule 5 to this Loan Agreement;

(d) "Deposit Account" means the account referred to in paragraph 4 of Schedule 3 to this Loan Agreement;

(e) "Eligible Items" means the goods imported under the Program (except those specifically excluded pursuant to the Attachment to Schedule 3 to this Loan Agreement), the foreign exchange costs of which are eligible for financing out of the proceeds of the Loan;

(f) "EPPSO" means the Economic Policy, Planning and Statistics Office of the Borrower established as of 24 March 2003 and any successor thereto acceptable to ADB;

(g) "Implementing Agency" means any of the MOF, Combined Utilities Board, MEC or EPPSO;

(h) "MEC" means the Marshalls Energy Company, Inc. whose corporate charter was granted by the Cabinet of Ministers of the Borrower as of 2 February 1984 and any successor thereto acceptable to ADB;

(i) "MOE" means the Ministry of Education of the Borrower and any successor thereto;

(j) "MOF" means the Ministry of Finance of the Borrower and any successor thereto acceptable to ADB;

(k) "Policy Matrix" means the policy matrix as agreed between the Borrower and ADB, which sets forth actions accomplished or to be accomplished by the Borrower under Subprogram 1 and the Program Cluster and is attached to the Policy Letter;

(l) "PPMS" means the Program Performance Monitoring System, referred to in paragraph 10 of Schedule 5 to this Loan Agreement;

(m) "Program Agreement" means the agreement of even date herewith between ADB and MEC for implementation of the Program;

(n) "Program Cluster" has the meaning specified in Recital (A) to this Loan Agreement;

(o) "Program Executing Agency" means for the purposes and within the meaning of the Loan Regulations, MOF and any successor thereto acceptable to ADB, which is responsible for the carrying out of Subprogram 1 and the Program Cluster;

(p) "PSC" means the Program Steering Committee of the Borrower, as described in paragraph 2 of Schedule 5 to this Loan Agreement, or any successor thereto acceptable to ADB;

(q) "Repair and Maintenance Account" means the account to be established by MEC and funded by MEC for repair and maintenance of MEC equipment for power generation and distribution, referred to in paragraph 9 of Schedule 5 to this Loan Agreement;

(r) "Sinking Fund Account" means the account to be established by the Borrower and funded by MEC to support the repayment obligations of the Borrower under this Loan Agreement, referred to in paragraph 7 of Schedule 5 to this Loan Agreement;

(s) "Subprogram 1 Period" means the period from 1 April 2009 through 31 August 2010;

(t) "Subsidiary Loan Agreement" means the loan agreement between the Borrower and MEC as described in paragraph 6 of Schedule 5 to this Loan Agreement under which the Borrower onlends a portion of the Counterpart Funds to MEC; and

(u) "TRAM" means the Tax Reform and Modernization Commission established by MOF.

ARTICLE II

The Loan

Section 2.01. ADB agrees to lend to the Borrower from ADB's Special Funds resources an amount in various currencies equivalent to six million four hundred thirteen thousand Special Drawing Rights (SDR6,413,000).

Section 2.02. (a) The Borrower shall pay to ADB an interest charge at the rate of 1% per annum during the grace period, and 1.5% per annum thereafter, on the amount of the Loan withdrawn from the Loan Account and outstanding from time to time.

(b) The term "grace period" as used in paragraph (a) of this Section means the period prior to payment of the first principal amount of the Loan on the payment date in accordance with the amortization schedule set forth in Schedule 2 to this Loan Agreement.

Section 2.03. The interest charge and any other charge on the Loan shall be payable semiannually on 15 February and 15 August in each year.

Section 2.04. The Borrower shall repay the principal amount of the Loan withdrawn from the Loan Account in accordance with the amortization schedule set forth in Schedule 2 to this Loan Agreement.

Section 2.05. The currency of repayment of the principal of the Loan and the currency of payment of the interest charge for the purposes of Sections 4.03(a) and 4.04 of the Loan Regulations shall be the Dollar.

ARTICLE III

Use of Proceeds of the Loan

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

Section 3.02. The proceeds of the Loan may be withdrawn from the Loan Account only for the purposes of financing foreign currency expenditures incurred for Eligible Items under the Program in accordance with the provisions of Schedule 3 to this Loan Agreement as such Schedule may be amended from time to time by agreement between the Borrower and ADB.

Section 3.03. Except as ADB may otherwise agree, all Eligible Items to be financed out of the proceeds of the Loan shall be procured in accordance with the provisions of Schedule 4 to this Loan Agreement.

Section 3.04. Withdrawals from the Loan Account shall be made only on account of expenditures relating to Eligible Items which:

(a) are produced in, and are 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 Loan Closing Date for the purposes of Section 8.02 of the Loan Regulations shall be 28 February 2011 or such other date as may from time to time be agreed between the Borrower and ADB.

ARTICLE IV

Particular Covenants

Section 4.01. In the carrying out of the Program, the Borrower shall perform, or cause to be performed, all obligations set forth in Schedule 5 to this Loan Agreement.

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

(b) The Borrower 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 6.05 of the Loan Regulations, the Borrower 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 and/or the Program Cluster, 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 6.05 of the Loan Regulations, the Borrower shall furnish, or cause to be furnished, to ADB quarterly 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

Suspension; Cancellation; Acceleration of Maturity

Section 5.01. The following are specified as additional events for suspension of the right of the Borrower to make withdrawals from the Loan Account for the purposes of Section 8.01(m) of the Loan Regulations:

(a) the charter or other constitutive documents of MEC shall have been repealed, suspended or amended in any manner which, in the reasonable opinion of ADB, will or may adversely affect the carrying out of the Program or the ability of MEC to perform any of its obligations under the Program Agreement; and

(b) MOF or MEC shall have failed to perform any of their respective obligations under the Subsidiary Loan Agreement.

Section 5.02. The following is specified as an additional event for acceleration of maturity for the purposes of Section 8.07(d) of the Loan Regulations: any of the events specified in Section 5.01 of this Loan Agreement shall have occurred.

ARTICLE VI

Effectiveness

Section 6.01. The following are specified as additional conditions to the effectiveness of this Loan Agreement for the purposes of Section 9.01(f) of the Loan Regulations:

(a) the Deposit Account, and the Sinking Fund Account shall have been opened as provided, respectively, in paragraph 4 of Schedule 3 to this Loan Agreement;

(b) the Program Agreement shall have been duly authorized or ratified by, executed and delivered by MEC;

(c) the Subsidiary Loan Agreement, in form and substance satisfactory to ADB, shall have been duly authorized or ratified by, executed and delivered by each of MOF and MEC; and

(d) all reform actions and measures relating to the Program, as specified under Policy Actions under Subprogram 1 Single Tranche Release of the Policy Matrix, shall have been taken or achieved and shall have been completed in a manner satisfactory to ADB.

Section 6.02. The following is specified as an additional matter, for the purposes of Section 9.02(d) of the Loan Regulations, to be included in the opinion or opinions to be furnished to ADB: each of the Program Agreement and the Subsidiary Loan Agreement shall have been duly authorized or ratified by, executed and delivered on behalf of MEC (for the Program Agreement) and MOF and MEC (for the Subsidiary Loan Agreement), and is legally binding upon MEC and, as applicable, MOF, in accordance with its terms.

Section 6.03. A date 90 days after the date of this Loan Agreement is specified for the effectiveness of the Loan Agreement for the purposes of Section 9.04 of the Loan Regulations.

ARTICLE VII

Miscellaneous

Section 7.01. The Minister of Finance of the Borrower is designated as representative of the Borrower for the purposes of Section 11.02 of the Loan Regulations.

Section 7.02. The following addresses are specified for the purposes of Section 11.01 of the Loan Regulations:

For the Borrower

Minister of Finance
Ministry of Finance
P.O. Box D
Majuro, Marshall Islands 96960

Telephone Numbers:

+692 625 7017
+692 625 7420.

Facsimile Number:

+692 625 3607.

For ADB

Asian Development Bank
6 ADB Avenue
Mandaluyong City
1550 Metro Manila
Philippines


Facsimile Numbers:

+63 2 636 2444
+63 2 636 2388.

IN WITNESS WHEREOF the parties hereto, acting through their representatives thereunto duly authorized, have caused this Loan 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.

REPUBLIC OF THE MARSHALL
ISLANDS

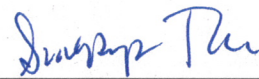
By



JACK J. ADING
Minister of Finance

ASIAN DEVELOPMENT BANK

By

_____
SUNGSUP RA
Director

Pacific Operations Division
Pacific Department

SCHEDULE 1

Description of the Program

1. The principal objectives of the Program Cluster, including the Program, are to:
 - (a) improve the medium term fiscal outlook, with a view to increasing the budget surplus;
 - (b) restrain public expenditure through selected reductions and freezes in selected major recurrent expenditure items;
 - (c) reform and modernize the tax system, including by introducing a sales tax, and by improving tax administration;
 - (d) improve the operational and financial performance of state owned enterprises (SOEs) through introduction of a national SOE policy and related legislation, and to implement a recovery plan for MEC; and
 - (e) support stakeholder participation and consultation in respect of the Program.
2. The Program Cluster is being implemented in the period from 1 April 2009 to 31 August 2013 and is described in more detail in the Policy Letter and the Policy Matrix.
3. The Program is the first of 2 subprograms in the Program Cluster and is being implemented during the Subprogram 1 Period. The reform agenda for the subsequent subprogram will be jointly refined by the Borrower and ADB to reflect the progress made under the Program and the evolving circumstances in the Borrower's economic management and public fiscal development.
4. In support of the Program:
 - (a) the proceeds of the Loan 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 other activities consistent with the objectives of the Program, pursuant to the provisions of paragraph 5 of Schedule 5 to this Loan Agreement.
5. The proceeds of the Loan are expected to be disbursed in a single tranche as soon as reasonably practicable following the Effective Date.

SCHEDULE 2**Amortization Schedule****(Public Sector Program - Subprogram 1)**

<u>Date Payment Due</u>	<u>Payment of Principal</u> (expressed in Special Drawing Rights)*
15-Feb-2019	200,406
15-Aug-2019	200,406
15-Feb-2020	200,406
15-Aug-2020	200,406
15-Feb-2021	200,406
15-Aug-2021	200,406
15-Feb-2022	200,406
15-Aug-2022	200,406
15-Feb-2023	200,406
15-Aug-2023	200,406
15-Feb-2024	200,406
15-Aug-2024	200,406
15-Feb-2025	200,406
15-Aug-2025	200,406
15-Feb-2026	200,406
15-Aug-2026	200,406
15-Feb-2027	200,406
15-Aug-2027	200,406
15-Feb-2028	200,406
15-Aug-2028	200,406
15-Feb-2029	200,406
15-Aug-2029	200,406
15-Feb-2030	200,406
15-Aug-2030	200,406
15-Feb-2031	200,406
15-Aug-2031	200,406
15-Feb-2032	200,406
15-Aug-2032	200,406
15-Feb-2033	200,406
15-Aug-2033	200,406
15-Feb-2034	200,406
15-Aug-2034	<u>200,414</u>
TOTAL	<u>6,413,000</u>

* The figures in this column represent SDR equivalents determined as of the respective dates of withdrawal. The arrangements for payment of each maturity are subject to the relevant provisions of the Special Operations Loan Regulations.

SCHEDULE 3

Withdrawal of Loan Proceeds

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

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

(b) No withdrawals from the Loan Account shall be made in respect of any expenditure which has been financed by credits from official international or bilateral aid agencies, or any other loans or grants made by ADB.

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

(b) Such withdrawal application shall be accompanied by a certificate of the Borrower confirming that: (i) in case the proceeds of the Loan will finance imports already made, the value of Eligible Imports in the period concerned exceeded the amount of the requested withdrawal; or (ii) in case the proceeds of the Loan will finance items to be imported, the value of Eligible Imports in the immediately preceding one-year period was greater than the amount of the requested withdrawal plus all other amounts expected to be withdrawn from the Loan Account during the succeeding one-year period. ADB will have the right to audit the use of the loan proceeds and verify the accuracy of the government's certification.

(c) For the purposes of this paragraph, the term "Eligible Imports" means the total imports of the Borrower 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 loans or grants made by ADB.

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

4. (a) All withdrawals from the Loan Account shall be deposited into an account of the Borrower at the Bank of Guam (BOG) nominated prior to the Effective Date by the Borrower (the "Deposit Account"). The Deposit Account shall be established, managed and liquidated in accordance with terms and conditions satisfactory to ADB.

Schedule 3

(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 Borrower shall have the Deposit Account or the Sinking Fund 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 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 Borrower shall submit trade statistics and any other information as ADB may require from time to time to assess the Borrower's compliance with the formula for determining Eligible Imports.

5. The Loan proceeds shall be disbursed in a single tranche upon effectiveness of this Loan Agreement.

6. Notwithstanding any other provisions of this Loan Agreement or the Loan Regulations and except as ADB may otherwise agree, no withdrawals shall be made from the Loan Account unless ADB shall be satisfied, based on evidence satisfactory to ADB and after consultation with the Borrower, that there has been no action which materially reverses the objectives of the Program.

7. Notwithstanding any other provisions of this Loan Agreement or the Loan Regulations and except as ADB may otherwise agree, no withdrawals shall be made from the Loan Account unless and until the documentary arrangements among the Borrower, MEC and BOG concerning the making of automatic transfers into the Sinking Fund Account and the Repair and Maintenance Account from revenue accounts of MEC, as described in paragraphs 7 and 9, respectively, of Schedule 5 to this Loan Agreement, shall have been concluded in form and substance satisfactory to ADB.

List of Ineligible Items

1. Loan proceeds will finance the foreign currency expenditures for the reasonable cost of imported goods required during the Program.
2. No withdrawals will be made for the following:
 - (a) 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 Borrower:

Table: 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.

- (b) expenditures in the currency of the Borrower or of goods supplied from the territory of the Borrower;
- (c) 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;
- (d) expenditures for goods intended for a military or paramilitary purpose or for luxury consumption;
- (e) expenditures for narcotics;
- (f) expenditures for environmentally hazardous 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; and

Attachment to Schedule 3

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

SCHEDULE 4

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 Loan.

2. (a) Except as provided in subparagraph (b) of this paragraph, 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 Borrower's prescribed procurement procedures, in the case of procurement by the public sector, having due regard for 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 5

Program Implementation and Other Matters

Program Management

1. MOF, as the Program Executing Agency, shall be responsible for: (a) overseeing all policy, legal and regulatory actions to be undertaken in connection with the Program; and (b) ensuring that all policy reforms set out in the Policy Letter and Policy Matrix are duly carried out in a timely manner. MOF shall also be responsible for the overall implementation of the Program Cluster and the Program, including reporting to ADB, administering and disbursing the Loan proceeds, and maintaining Program records and accounts. MOF shall, through suitable staff, be responsible for day-to-day implementation of the Project including: (a) coordinating the activities of consultants; (b) overseeing the implementation of the Program; (c) monitoring the social, gender and economic impact of Program implementation; (d) supervising government reform and capacity development activities; and (e) preparing and consolidating accounting, auditing, and monitoring reports as required for submission to ADB.

2. PSC, comprising officials from MOF, the Ministry of Resources and Development of the Borrower (MOR), Chief Secretary on behalf of the Cabinet, the Ministry of Public Works of the Borrower, the Public Service Commission of the Borrower, and MEC, shall function as the Program steering committee and shall be responsible for overseeing the implementation of the Program. The PSC shall meet at least every quarter year to monitor progress, oversee implementation, and provide guidance and direction to the Program Executing Agency. The PSC shall invite concerned line agencies of the Borrower as well as ADB, other donor partners and other relevant stakeholders to participate in meetings to discuss Program Cluster and the Program implementation issues.

Implementation of the Policy Letter

3. The Borrower shall:

(a) ensure that the policies adopted and actions taken prior to the date of this Loan Agreement as described in the Policy Letter and the Policy Matrix, continue in effect for the duration of the Program Period and subsequently; and

(b) promptly adopt all other policies and take all other actions as described in the Policy Letter and 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 Borrower shall:

(a) keep ADB informed of, and the Borrower and ADB shall from time to time exchange views on, sector issues, policy reforms and additional reforms during the Program Cluster implementation period and the Subprogram 1 Period that may be considered necessary or desirable, including the progress made in carrying out policies and actions set out in the Policy Letter and the Policy Matrix;

Schedule 5

(b) promptly discuss with ADB problems and constraints encountered during implementation of the Program and appropriate measures to overcome or mitigate such problems and constraints;

(c) participate in the regular meetings of the joint working group consisting of key development partners engaged in the Borrower's public sector reforms consisting of the U.S., Australia, Japan, the European Union (EU), Taipei, China, the World Bank, the International Monetary Fund (IMF) and ADB; and

(d) keep ADB informed of policy discussions with other multilateral or bilateral agencies that have implications for implementation of the Program Cluster and Subprogram 1 and shall provide ADB with an opportunity to comment on any resulting policy proposals. The Borrower shall take ADB's views into consideration before finalizing or implementing any such proposals.

Counterpart Funds

5. The Borrower shall ensure that the Counterpart Funds are used to finance the local currency costs relating to public expenditure objectives under the Program and that the necessary budget appropriations and adequate resources are allocated and released in a timely manner in order to ensure effective implementation of the Program and other activities consistent with the objectives of the Program Cluster.

Rationalization of MEC

6. The Borrower shall ensure that the Subsidiary Loan Agreement, in form and substance satisfactory to ADB, is executed by and between MOF and MEC as a condition to effectiveness hereunder. The Borrower shall onlend to MEC a portion of the Counterpart Funds generated by the Loan under the Subsidiary Loan Agreement for the purpose of restructuring its outstanding commercial debt with the Bank of Guam (BOG) and shall ensure that such funds are so applied.

7. (a) The Borrower, through MOF, shall establish the Sinking Fund Account at BOG to accumulate funds to service its repayment obligations under this Loan Agreement. The Sinking Fund Account shall be established, managed and liquidated in accordance with terms and conditions satisfactory to ADB. No payments, transfers or deductions shall be authorized, permitted, or made out of the Sinking Fund Account other than for the purpose of servicing the repayment obligations of the Borrower under this Loan Agreement commencing with the first date set forth on the amortization schedule in Schedule 2 to this Loan Agreement, and the Borrower and ADB shall enter into documentary arrangements with BOG, satisfactory to ADB, establishing that no such payments, transfers or deductions may be made out of the Sinking Fund Account without the written approval of ADB or its designated representative. Such Sinking Fund Account shall be subject to annual audit by MOF and ADB to ensure its use for the intended purposes.

(b) MOF shall ensure, including through provisions in the Subsidiary Loan Agreement, and MEC shall undertake, that MEC shall make automatic monthly payments into the Sinking Fund Account from its revenue accounts in the amount of no less than \$33,279 (thirty-three thousand two hundred seventy-nine Dollars) commencing immediately following restructuring of the outstanding sovereign-guaranteed indebtedness of MEC with

BOG. MEC shall authorize BOG and any or all other institutions holding its accounts, as applicable, to carry out such automatic transfers pursuant to documentary arrangements satisfactory to MOF and ADB.

(c) MOF shall ensure that MEC shall enter into, and MEC undertakes to enter into, arrangements concerning its assets including accounts with BOG (and other institutions as applicable), in form and substance satisfactory to ADB, which shall give MOF the first priority right to receive payments from other assets of MEC, including grants or donor assistance payable to MEC, or to withhold payments or subsidies to MEC from the RMI budget, in the event of a default in the obligation of MEC to contribute to the Sinking Fund Account, which shall be continuing for at least 15 days following the due date therefor.

8. Such Sinking Fund Account and the arrangements concerning them shall be without prejudice to, and without limitation on, the obligations of the Borrower under this Loan Agreement.

Repair and Maintenance Account

9. The Borrower and MOF shall ensure that the Subsidiary Loan Agreement will require MEC to, and MEC shall, pursuant to the Program Agreement, undertake to and shall, (a) open a separate bank account at BOG dedicated to repair and maintenance funds (the "Repair and Maintenance Account"); (b) make automatic monthly payments into the Repair and Maintenance Account from its revenue accounts in the amount of no less than thirty-five thousand Dollars (\$35,000) commencing immediately following restructuring of the outstanding sovereign-guaranteed indebtedness of MEC with BOG; and (c) authorize BOG and any or all other institutions holding its accounts, as applicable, to carry out such automatic transfers pursuant to documentary arrangements satisfactory to MOF and ADB. Funds in the Repair and Maintenance Account shall be used exclusively for repair, maintenance, procurement of spare parts, materials and equipment (and related labor costs) directly related to power generation and distribution. Such Repair and Maintenance Account shall be subject to annual audit by MOF and ADB to ensure its use for the intended purposes.

Monitoring of the Program and Subsequently

10. The Borrower shall ensure that MOF is responsible for: (a) establishing and maintaining a PPMS in a form and with a composition acceptable to ADB within 3 months after the Effective Date; (b) carrying out monitoring and evaluation of the Program, for at least 1 year after completion of the Program, or the Program Cluster (whichever is later); and (c) maintaining all relevant monitoring data to evaluate the benefits of the Program. Specific performance indicators, as agreed with ADB, shall be used to assist with monitoring the implementation of policy actions and their impact on budget outcomes and public enterprise performance (including financial and performance indicators).

11. The Borrower shall ensure that reporting on the progress of the Program through periodic meetings at least every 6 months is made by MOF to ADB in accordance with the performance indicators described in the preceding paragraph.

12. The Borrower and ADB shall jointly conduct periodic reviews of the macroeconomic and fiscal conditions of the Borrower's economy and assess the impact and

evaluate the benefits of the Program and the Program Cluster, in accordance with the PPMS. The Borrower shall cause the MOF to submit a Program completion report to ADB within 3 months after the Program Cluster implementation period that assesses compliance with, and the impact of, the agreed actions under the Program on each sector and describes lessons identified during the Program Period. The Borrower and ADB may use the findings of such assessment and evaluation to refine the Program Cluster.

Anticorruption

13. The Borrower, the Program Executing Agency, and the Implementing Agencies shall (a) comply with ADB's *Anticorruption Policy* (1998, as amended to date), and acknowledge that ADB reserves the right to investigate directly or through its agents, any alleged corrupt, fraudulent, collusive or coercive practices relating to the Program; and (b) cooperate with any such investigation and extend all necessary assistance, including providing access to all relevant books and records for the satisfactory completion of such investigation. The Borrower shall undertake necessary measures to create and sustain a corruption-free environment; ensure that its anticorruption law and regulations as well as ADB's *Anticorruption Policy* (1998, as amended to date) are strictly enforced and complied with during Program implementation, including ensuring the right of ADB to audit and examine the records and accounts of the Program Executing Agency and the Implementing Agencies as they relate to the Program.