

ISLAMIC REPUBLIC OF PAKISTAN
Sindh Devolved Social Services Program


MINUTES OF LOAN NEGOTIATIONS

INTRODUCTION

1. Loan negotiations for the proposed Sindh Devolved Social Services Program (Program) were held at the Pakistan Resident Mission of the Asian Development Bank (ADB) from 13 to 15 November, 2003 between the representatives of the Borrower (the Borrower), the Province of Sindh (Sindh) of the first part and ADB of the other part.

2. The Borrower and Sindh were represented by the following officials (Borrower Team):

Mr. Malik Asrar Hussain Secretary, Finance Department, Sindh	-	Chief Negotiator
Mr. M. Ashraf Khan Joint Secretary, Economic Affairs Division	-	Member
Mr. Ghulam Sarwar Khero Additional Chief Secretary (Development) Planning and Development Department, Sindh	-	Member
Mr. Ghulam Ali Pasha Secretary, Education Department, Sindh	-	Member
Mr. M. Nawaz Leghari Special Secretary, Finance Department, Sindh	-	Member
Mr. Sualeh A. Faruqi Secretary, Sindh Local Government Board Local Government Department, Sindh	-	Member
Mr. Abdul Kabir Kazi Additional Secretary Finance Department, Sindh	-	Member
Mr. M. Umer Abro Additional Director (Development) Health Department, Sindh	-	Member
Dr. Javed Ahktar Shaikh SAP Coordinator (Health) Health Department, Sindh	-	Member
Mr. Nadeem Mahbub Section Officer, Economic Affairs Division	-	Member

3. ADB was represented by the following officers (ADB Team):

Mr. Vincent de Wit Sr. Health Specialist Development & Planning Specialis	-	Chief Negotiator
Mr. M. Ali Shah Country Director, PRM	-	Member (on stand-by basis)
Ms. Aysha Qadir Counsel	-	Member
Mr. Safdar Parvez Programs Officer, PRM	-	Member
Ms. R. Rasuman Sr. Financial Control Specialist	-	Member (on stand-by basis in Headquarters)
Mr. Shahid Kardar ADB Consultant	-	Observer
Mr. Farrukh Moriani ADB Consultant	-	Observer

4. Copies of the draft: (i) Program Loan Agreement (Ordinary Operations); (ii) Program Loan Agreement (Special Operations); (iii) Program Agreement; (iv) Technical Assistance Loan Agreement (Special Operations); and (v) Project Agreement (individually "Loan Document" and collectively "Loan Documents"), which had earlier been provided to the Borrower Team formed the basis for the negotiations. Three copies of each of the draft Loan Documents, incorporating the agreed changes, were initialed on behalf of the Borrower, Sindh, and ADB with one copy of each of the initialed Loan Documents being retained by the Borrower, Sindh, and ADB. The draft Loan Documents, as negotiated and agreed upon, are attached hereto as Appendices 1, 2, 3, 4 and 5, respectively. Unless otherwise defined herein, capitalized terms used in these Minutes shall have the same meanings ascribed thereto in the Loan Documents.

5. These Minutes record certain matters of clarification and interpretation relating to the Report and Recommendation of the President (RRP) and the Loan Documents, and also state the agreement of the Borrower Team and the ADB Team on certain aspects of the Program implementation.

GENERAL

6. The ADB Team explained ADB's policy on confidentiality and disclosure of information, and informed the Borrower Team that, according to this policy, the RRP will be declassified and made available to the general public on request following approval of the Program by ADB's Board of Directors. The draft RRP had been submitted to the Borrower Team for review, and the Borrower Team indicated that the RRP did not contain information or data that is of a sensitive or confidential nature.

7. The ADB Team brought to the attention of the Borrower Team ADB's Anti-Corruption Policy. In particular, attention was drawn to ADB's policy to require borrowers of ADB loans as well as bidders/suppliers/contractors/consultants under contracts financed through ADB loans to observe the highest standards of ethics during the procurement and execution of such contracts. The anti-corruption provision of the *Guidelines for Procurement under Asian Development Bank Loans, Guidelines on the Use of Consultants by Asian Development Bank and Its Borrowers, Ordinary Operations Loan Regulations Applicable to LIBOR-Based Loans Made from ADB's Ordinary Capital Resources* and the *Special Operations Loan Regulations of ADB* were specifically brought to the attention of the Borrower Team.

8. The Borrower Team acknowledged that the disbursement procedures set out in the ADB's *Loan Disbursement Handbook 2001* are supplemented by the *Interim Guidelines for Disbursement, LIBOR-Based Loan Products* dated July 2002.

PROGRAM LOAN AGREEMENT (ORDINARY OPERATIONS)

Sections 2.01 and 2.02

9. The Borrower Team confirmed that the Borrower has chosen to borrow in Yen. The proposed Yen amount of the loan is ¥11,968,550,000 (OCR Loan), equivalent to US\$110,000,000, computed at the conversion rate of ¥108.805 equaling US\$1.00, which is the conversion rate for ADB's transactions on the last working day (i.e. 14 November 2003) of the loan negotiations.

10. The Borrower Team strongly requested the ADB Team as to whether the term of the OCR Loan could be 25 years including a grace period of 5 years as a special case. The ADB Team informed the Borrower Team and the Borrower Team accepted that Ordinary Capital resources loans have a standard term of 15 years including a grace period of 3 years. It was noted that the amount of a fixed spread expressed in percentage per annum (currently 0.60%), will be determined on the date of signing of the Program Loan Agreement (Ordinary Operations) and communicated to the Borrower.

11. The Borrower Team informed the ADB Team that the Borrower's decision to borrow under the ADB's *Ordinary Operations Loan Regulations Applicable to LIBOR-Based Loans Made from ADB's Ordinary Capital Resources* dated 1 July (LBL Facility) has been based on the Borrower's informed opinion that the LBL Facility on the financial terms described in the draft Program Loan Agreement (Ordinary Operations) most appropriately provides the Borrower with the ability to manage the risk exposures under the Program as well as the Borrower's external debt portfolio.

12. The Borrower Team acknowledged to the ADB Team that:

(a) The Borrower has made its own independent decision to borrow under the LBL Facility on the terms set out above and in the draft Program Loan Agreement (Ordinary Operations) for the Program and is not relying on any communication or confirmation from ADB as a recommendation with respect thereto; and

(b) ADB is not acting as an advisor to the Borrower in respect of the Borrower's choice of loan terms for the Program.

Section 2.03

13. The Borrower Team queried the rationale for having the commitment charge accrue at the rate of 0.75% per annum on the unwithdrawn amount of the proposed OCR Loan. The ADB Team responded that while it understood the Borrower Team's query, the application of the commitment charge is standard across all loans provided by ADB to borrowers from ADB's Ordinary Capital resources. While indicating that this Section could not be negotiated, the ADB Team agreed to bring this issue to the attention of the ADB's Management.

Section 2.04

14. The Borrower Team also queried the rationale for the Borrower's obligation to pay a front-end fee of 0.50% of the amount of the proposed OCR Loan. The ADB Team responded that while it understood the Borrower Team's query, the application of the front-end fee is standard across all loans provided by ADB to borrowers from ADB's Ordinary Capital resources.

15. The ADB Team advised the Borrower Team that ADB's Board of Directors has approved a 0.50% reduction in front-end fee charged on all OCR public sector loans approved in 2003. Considering the proposed schedule for Board consideration of the Program, the ADB Team and the Borrower Team agreed that (i) the OCR Loan will be charged a front-end fee of 0.50% provided it is approved in 2003; and (ii) in the event the OCR Loan is not approved in 2003: (A) the front-end fee will revert to 1.0% (subject to adjustment when the Board determines the appropriate front-end fee to be charged for OCR public sector loans approved after 2003); and (B) the Borrower hereby authorizes ADB to make the necessary changes to the Program Loan Agreement (Ordinary Operations).

PROGRAM LOAN AGREEMENT (SPECIAL OPERATIONS)Section 2.01

16. The proposed loan amount equivalent to US\$100,000,000 (ADF Loan) was converted, consistent with ADB's policy of denominating Special Funds Loans in Special Drawing Rights (SDR), to SDR 69,843,000 at the conversion rate of SDR 1.00 equaling US\$1.43178, which is the conversion rate for ADB's transactions on the last working day (i.e. 14 November 2003) of the loan negotiations. Such conversion was made elsewhere as required in the draft Program Loan Agreement (Special Operations).

17. The ADB Team advised the Borrower Team that in view of the shortage of the ADF resources available under Expanded Commitment Authority and pending the availability of further ADF commitment authority, the Board has adopted the conditional approval procedure for several ADF loans. The condition attached to such a loan approval is that the loan agreement will not be signed until the President has determined that ADB has sufficient ADF resources to cover the ADF Loan. ADB will advise the Borrower of when the ADF resources will be available and the timing of loan signing.

Section 2.04(b)

18. The ADB Team informed the Borrower Team that pursuant to ADB's Graduation Policy, ADB's per capita GNP operational cutoff in respect of ADB's Special

Funds resources has been amended to be harmonized with the International Development Association's per capita GNP operational cutoff. The Project Loan Agreement (Special Operations) reflects ADB's new policy of annually updating the per capita GNP operational cutoff. The current per capita GNP operational cutoff is US\$865 in 2002 prices.

COMMON MINUTES TO LOAN DOCUMENTS

Tranching

19. The Borrower Team requested revised distribution of ADF and OCR shares across the 3 tranches, with equal shares of ADF spread across the 3 years in view of the timing of the first tranche in the middle of the fiscal year, and capacity constraints. The overall size of the tranches was maintained at respectively \$100,000,000, \$70,000,000 and \$40,000,000. The ADB Team accepted this request and made requisite amendments in the Loan Documents and the RRP.

Repayment Dates

20. The Borrower Team confirmed that the Borrower has chosen 15 March and 15 September as repayment dates in each year.

Relending Terms

21. The Borrower Team informed the ADB Team and the ADB Team noted that the Borrower shall relend the proceeds of the loans to Sindh on the same terms and conditions as are applicable to the Borrower and that the foreign exchange risk shall be borne by Sindh. Sindh confirmed to the ADB Team that such terms and conditions are acceptable to Sindh.

Development Policy Letter, Policy Matrix and Attachments 2, 3 and 4 to Schedule 3 of the Program Loan Agreement (Ordinary Operations) and the Program Loan Agreement (Special Operations)

22. The ADB Team received the revised Development Policy Letter, which was considered acceptable to the ADB Team. The signed Development Policy Letter is attached hereto as Appendix 6. Tranche conditions specified in the Policy Matrix were discussed and the agreed Policy Matrix is attached hereto as Appendix 7. Attachments 2, 3 and 4 to Schedule 3 of the Program Loan Agreement (Ordinary Operations) and the Program Loan Agreement (Special Operations) were revised accordingly.

Executing Agency

23. The Borrower Team requested the ADB Team for a change in the Executing Agency from the SP&DD to the Finance Department, Sindh. While this was considered a substantial change in the Program design, the Borrower Team provided strong justification, and the ADB Team accepted this change.

24. In this context, the Borrower Team pointed out that the Finance Department has substantial internal staff capacity and will not require the services of an international consultant as a Co-director for the Program. The Borrower Team and the ADB Team agreed that the possibility of engagement of an international consultant will be retained for now and reviewed at the Program Inception Mission. Similarly, other consulting

services provided under the TA Loan (as defined below) will also be reviewed to assess the need for adjustments in consulting services. The Borrower Team agreed with this arrangement.

Auditing and Reporting Requirements

25. The Borrower Team informed the ADB Team that expect for the Deposit Account to be opened by the Borrower with SBP into which all withdrawals from the Loan Account shall be deposited, Sindh cannot maintain separate accounts for the OCR Loan and the ADF Loan and have such accounts and related financial statements audited annually, etc., by independent auditors acceptable to ADB, since the proceeds of the Program loans will be deposited in Account No. 1 of Sindh. Confirmation from the Sr. Financial Control Specialist was sought on this issue, who informed that for program lending, provincial governments may not be required to maintain separate accounts and have such accounts audited, and such requirements are generally restricted to the Deposit Account. Upon such confirmation, the ADB Team deleted the provisions set out in the Program Loan Agreement (Ordinary Operations), the Program Loan Agreement (Special Operations) and the Program Agreement, whereunder Sindh was required to maintain separate accounts for the OCR Loan and the ADF Loan and have such accounts audited annually.

PROGRAM AGREEMENT

Section 2.10

26. On the query of the Borrower Team, the ADB Team confirmed that in case ADB representatives inspect the Program, the goods financed out of the proceeds of the Program loans and any relevant records and documents, the expenses incurred in connection with such inspection shall be borne by ADB.

TECHNICAL ASSISTANCE LOAN AGREEMENT (SPECIAL OPERATIONS)

Section 2.01

27. The proposed loan amount equivalent to US\$10,000,000 (TA Loan) was converted, consistent with ADB's policy of denominating Special Funds Loans in Special Drawing Rights (SDR), to SDR 6,984,000 at the conversion rate of SDR 1.00 equaling US\$1.43178, which is the conversion rate for ADB's transactions on the last day of loan negotiations. Such conversion was made elsewhere as required in the draft Technical Assistance Loan Agreement (Special Operations).

28. The ADB Team advised the Borrower Team that in view of the shortage of the ADF resources available under Expanded Commitment Authority and pending the availability of further ADF commitment authority, the Board has adopted the conditional approval procedure for several ADF loans. The condition attached to such a loan approval is that the loan agreement will not be signed until the President has determined that ADB has sufficient ADF resources to cover the TA Loan. ADB will advise the Borrower of when the ADF resources will be available and the timing of loan signing.

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Section 2.04(b)

29. The ADB Team informed the Borrower Team that pursuant to ADB's Graduation Policy, ADB's per capita GNP operational cutoff in respect of ADB's Special Funds resources has been amended to be harmonized with the International Development Association's per capita GNP operational cutoff. The Project Loan Agreement (Special Operations) reflects ADB's new policy of annually updating the per capita GNP operational cutoff. The current per capita GNP operational cutoff is US\$865 in 2002 prices.

GENERAL


30. Sindh strongly requested the ADB Team for additional assistance of \$150,000,000 in 2004 for public resource management to help address Sindh's fiscal constraints. The ADB Team informed the Borrower Team that this matter has already been brought to the attention of the ADB's Management. The ADB Team informed the Borrower Team that ADB has agreed to consider Sindh's request for additional assistance in 2004, and the amount of such assistance will be determined after ADB's internal review of the matter. The Borrower Team confirmed that this possible additional assistance from ADB would not replace SAC and would help sustain increased social sector financing initiated under the Program as part of the Poverty Reduction Strategy.

31. The following Appendices are attached to these Minutes:

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| Appendix 1 | - | Program Loan Agreement (Ordinary Operations) |
| Appendix 2 | - | Program Loan Agreement (Special Operations) |
| Appendix 3 | - | Program Agreement |
| Appendix 4 | - | Technical Assistance Loan Agreement (Special Operations) |
| Appendix 5 | - | Project Agreement |
| Appendix 6 | - | Development Policy Letter |
| Appendix 7 | - | Policy Matrix |


Signed in Islamabad on 15 November 2003.

FOR THE ISLAMIC REPUBLIC
OF PAKISTAN



M. Ashraf Khan 17/11/2003
Signed in Manila

FOR THE ASIAN DEVELOPMENT
BANK



Vincent de Wit

FOR THE PROVINCE OF SINDH



Malik Asrar Hussain