June 05, 2013

Honourable Secretary Lam Dorji
Ministry of Finance
Royal Government of Bhutan
Tashichhodzong
Thimphu, Kingdom of Bhutan

Re: Kingdom of Bhutan: IDF Grant for Strengthening Intergovernmental
Fiscal Systems and Capacity Building Project
IDF Grant No. TF014439

Excellency:

In response to the request for financial assistance made on behalf of the Kingdom of Bhutan (“Bhutan”) or (“Recipient”), I am pleased to inform you that the International Bank for Reconstruction and Development (“World Bank”) proposes to extend to the Recipient, a grant from the World Bank’s Institutional Development Fund (“IDF”) in an amount not to exceed two hundred ninety thousand three hundred United States Dollars (U.S.$290,300) (“Grant”) on the terms and conditions set forth or referred to in this letter agreement (“Agreement”), which includes the attached Annex, to assist in the financing of the project described in the Annex (“Project”).

The Recipient represents, by confirming its agreement below, that it is authorized to enter into this Agreement and to carry out the Project in accordance with the terms and conditions set forth or referred to in this Agreement.

Please confirm the Recipient’s agreement to the foregoing by having an authorized official of the Recipient sign and date the enclosed copy of this Agreement, and returning it to the World Bank. Upon receipt by the World Bank of this countersigned copy, this Agreement shall become effective as of the date of the countersignature; provided, however, that the offer of this Agreement shall be deemed withdrawn if the World Bank has not received the countersigned copy of this Agreement within ninety (90) days after the date of signature of this
Agreement by the World Bank, unless the World Bank shall have established a later date for such purpose.

Very truly yours,

INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT

[Signature]

Anthony Cholst
Acting Country Director for Bhutan
South Asia Region

AGREED:
KINGDOM OF BHUTAN

[Signature]

By
Authorized Representative

Name: MR. LAM DORJI
Title: SECRETARY, MINISTRY OF FINANCE
Date: 10th July, 2013

Enclosures:

(2) Disbursement Letter of the same date as this Agreement, together with World Bank Disbursement Guidelines for Projects, dated May 1, 2006

Cc:
Mr. Choiten Wangchuk,
Director General,
Department of Public Accounts,
Ministry of Finance,
Royal Government of Bhutan
Thimphu, Bhutan
ANNEX

Article I
Standard Conditions; Definitions


1.02. *Definitions.* Unless the context requires otherwise, the capitalized terms used in this Agreement have the meanings ascribed to them in the Standard Conditions or in this Agreement as follows:

(a) "Department of National Budget" means the department responsible for national budgeting within the Ministry of Finance.

(b) "GNHC" means Gross National Happiness Commission.

(c) "Royal Audit Authority" is the supreme audit institution of the Recipient responsible to audit and report on the economy, efficiency and effectiveness in the use of public resources as per Article 25.1 of the Constitution of the Kingdom of Bhutan.

(d) "Royal Institute of Management" means the Recipient’s apex management training institute established in 1986 and incorporated as an autonomous institute in 1990 under the Royal Charter with a Board of Directors as its governing authority, and mandated to impart, promote and improve professional knowledge and skills in management and public administration in both public as well as private sectors.

(e) "Thromde Finance Committee" means the committee to be established by the Recipient within the Ministry of Finance to be responsible for the management of intergovernmental fiscal relations.

(f) "Training" means training activities related to the Project, attributable to courses, seminars and workshops, and comprising local and international travel costs and subsistence allowances for training participants, costs associated with securing the services of trainers and speakers, rental of training facilities, and preparation reproduction and dissemination of training materials, and other costs directly related to training preparation and implementation.

Article II
Project Execution

2.01. *Project Objectives and Description.* (a) The objective of the Project is to strengthen the capacities of (i) the Department of National Budget to design and implement a principle based intergovernmental fiscal system for Thromdes (urban local governments) in Bhutan; and (ii) the Thromdes in operationalizing the said system.

(b) The Project consists of the following parts:
1. **Strengthening Capacities of the Department of National Budgeting to Manage Intergovernmental Fiscal Relations**

Strengthening the capacities of the Department of National Budget to: (a) design and put in place a principle based system of intergovernmental transfer of finances to Thromdes; and (b) to design the appropriate institutional structures and rules of business for the Thromde Finance Committee, through a learning process involving: (i) the preparation of a compendium of country case studies and international good practices to inform policy makers on the issues and experiences of fiscal transfer design and implementation; (ii) conducting training and workshops to bring experienced academics and policy makers from selected countries for leaders and executives to learn from such country experiences, to facilitate discussions on reform of intergovernmental fiscal systems and to identify suitable institutional arrangements for designing Thromde finance committee; and (iii) exposure visits for policy makers and local governments to selected countries with effective intergovernmental fiscal systems.

2. **Design of a Principle Based Framework for the Allocation of Capital and Recurrent Grants**

(i) Design a principle based framework for the annual allocation of capital and recurrent grants to Thromdes for the purpose of identify existing gaps, through review of the current system of allocation of resources to Thromdes.

(ii) Design a customized intergovernmental fiscal system drawing lessons from the standard principles of fiscal transfer, established international good practices and stakeholder consultations, ensuring the system’s alignment to the fiscal transfer formulas devised by GNHC, as may be modified to suit the requirements of urban local governments.

(iii) Devise operating rules that will enable the Department of National Budget to link the fiscal transfer system to the annual planning and budgeting exercise.

(iv) Strengthen the capacity of the Department of National Budget to prepare a work plan for rolling out the new system including capacity building to the Thromdes.

(v) Strengthen the capacity of the Ministry of Finance to set up the Thromde Finance Committee, including the drafting of the terms of reference and operating procedures of the said committee.

3. **Strengthening the Procedures and Capacities for Municipal Budget and Financial Management**

(i) Strengthen the capacity of the Recipient to prepare guidelines and manuals for municipal budgeting and financial management in accordance with the redesigned intergovernmental fiscal system mentioned in parts 1 and 2 above. The said guidelines and manual will be used to train the municipal staff in the preparation of realistic capital investment proposals and annual plans to meet
Kingdom of Bhutan

revenue expenditures from their own sources, and prepare “How To” guides for specific aspects of the budget preparation process and other related topics, including capital expenditure monitoring and audits.

(ii) Provision of training to budget officers at the national and local levels and other related agencies, including the Royal Audit Authority in the revised guidelines and manuals and the annual budget preparation.

(iii) Establishment of a forum, including an online community of practice of municipal finance practitioners, for the continuous exchange of information and guidance between the central and local governments.

2.02. Project Execution Generally. The Recipient declares its commitment to the objectives of the Project. To this end, the Recipient shall carry out the Project through the Department of National Budget of the Ministry of Finance, in accordance with the provisions of: (a) Article II of the Standard Conditions; (b) the “Guidelines on Preparing and Combating Fraud and Corruption in Projects Financed by IBRD Loans and IDA Credits and Grants”, dated October 15, 2006 and revised in January 2011 (“Anti-Corruption Guidelines”); and (c) this Article II.

2.03. Institutional and Other Arrangements. (a) The Recipient shall be responsible for the overall implementation of the Project through the Department of National Budget.

(b) The Recipient shall coordinate with the Ministry of Works and Housing, the Thromdes and the Royal Institute of Management in the implementation of the Project.

2.04. Project Monitoring, Reporting and Evaluation. (a) The Recipient shall monitor and evaluate the progress of the Project and, upon the World Bank’s request, prepare Project Reports, in accordance with the provisions of Section 2.06 of the Standard Conditions and on the basis of indicators set forth in paragraph (b) below. Each Project Report shall cover such period as shall be indicated in the World Bank’s request and shall be furnished to the World Bank not later than forty-five (45) days after the date of such request.

(b) The Performance indicators referred to above in paragraph (a) above consist of the following:

(i) Senior policy makers of the Recipient trained in the concepts and practices of intergovernmental fiscal systems;

(ii) Annual budget allocations to Thromdes reformed and made principle based;

(iii) Decrease in variance/discrepancy between annual plans and budgets in each of the Thromdes.

(c) The Recipient shall, upon the World Bank’s request, prepare the Completion Report in accordance with the provisions of Section 2.06 of the Standard Conditions. The Completion Report shall be furnished to the World Bank not later than five (5) months after the Closing Date.
2.05. **Financial Management.** (a) The Recipient shall ensure that a financial management system is maintained in accordance with the provisions of Section 2.07 of the Standard Conditions.

(b) The Recipient shall ensure that interim unaudited financial reports for the Project are prepared and furnished to the World Bank not later than forty five (45) days after the end of each calendar quarter, covering the quarter, in form and substance satisfactory to the World Bank.

(c) The Recipient shall have its Financial Statements audited in accordance with the provisions of Section 2.07 (b) of the Standard Conditions. Each audit of the Financial Statements shall cover the period of one (1) fiscal year of the Recipient. The audited Financial Statements for each such period shall be furnished to the World Bank not later than six (6) months after the end of such period.

2.06. **Procurement**

(a) **General.** All goods and consultants' services required for the Project and to be financed out of the proceeds of the Grant shall be procured in accordance with the requirements set forth or referred to in:


(ii) Sections I and IV of the “Guidelines: Selection and Employment of Consultants under IBRD Loans and IDA Credits and Grants by World Bank Borrowers” dated January 2011 (“Consultant Guidelines”), in the case of consultants’ services; and

(iii) the provisions of this Section, as the same shall be elaborated in the procurement plan prepared and updated from time to time by the Recipient for the Project in accordance with paragraph 1.18 of the Procurement Guidelines and paragraph 1.25 of the Consultant Guidelines (“Procurement Plan”).

(b) **Definitions.** The capitalized terms used in the following paragraphs of this Section to describe particular procurement methods or methods of review by the World Bank of particular contracts, refer to the corresponding method described in Sections II and III of the Procurement Guidelines, or Sections II, III, IV and V of the Consultant Guidelines, as the case may be.

(c) **Particular Methods of Procurement of Goods.**

(i) Except as otherwise provided in sub-paragraph (ii) below, goods shall be procured under contracts awarded on the basis of International Competitive Bidding.
(ii) The following methods, other than International Competitive Bidding, may be used for procurement of goods for those contracts which are specified in the Procurement Plan: (A) Limited International Bidding; (B) National Competitive Bidding, subject to the additional provisions set forth in the Appendix to this Annex; (C) Shopping; (D) Direct Contracting; and (E) Community Participation procedures which have been found acceptable to the World Bank.

(d) Particular Methods of Procurement of Consultants' Services

(i) Except as otherwise provided in item (ii) below, consultants' services shall be procured under contracts awarded on the basis of Quality- and Cost-based Selection.

(ii) The following methods may be used for the procurement of consultants' services for those assignments which are specified in the Procurement Plan: (A) Quality-based Selection; (B) Selection under a Fixed Budget; (C) Least Cost Selection; (D) Selection based on Consultants' Qualifications; (E) Single-source Selection of consulting firms; (F) Selection of Individual Consultants; and (G) Single-source procedures for the Selection of Individual Consultants.

(e) Review by the World Bank of Procurement Decisions. The Procurement Plan shall set forth those contracts which shall be subject to the World Bank's Prior Review. All other contracts shall be subject to Post Review by the World Bank.

Article III
With regard to the Withdrawal of Grant Proceeds

3.01. Eligible Expenditures. The Recipient may withdraw the proceeds of the Grant in accordance with the provisions of: (a) Article III of the Standard Conditions; (b) this Section; and (c) such additional instructions as the World Bank may specify by notice to the Recipient (including the “World Bank Disbursement Guidelines for Projects” dated May 2006, as revised from time to time by the World Bank and as made applicable to this Agreement pursuant to such instructions), to finance Eligible Expenditures as set forth in the following table. The table specifies the categories of Eligible Expenditures that may be financed out of the proceeds of the Grant (“Category”), the allocations of the amounts of the Grant to each Category, and the percentage of expenditures to be financed for Eligible Expenditures in each Category:
<table>
<thead>
<tr>
<th>Category</th>
<th>Amount of the Grant Allocated (expressed in USD)</th>
<th>Percentage of Expenditures to be Financed (inclusive of Taxes)</th>
</tr>
</thead>
<tbody>
<tr>
<td>(1) Goods</td>
<td>8,000</td>
<td>100%</td>
</tr>
<tr>
<td>(2) Consultants' Services</td>
<td>195,700</td>
<td>100%</td>
</tr>
<tr>
<td>(3) Training</td>
<td>86,600</td>
<td>100%</td>
</tr>
<tr>
<td><strong>TOTAL AMOUNT</strong></td>
<td><strong>290,300</strong></td>
<td></td>
</tr>
</tbody>
</table>

3.02. **Withdrawal Conditions.** Notwithstanding the provisions of Section 3.01 of this Agreement, no withdrawal shall be made for payments made prior to the date of countersignature of this Agreement by the Recipient.

3.03. **Withdrawal Period.** The Closing Date referred to in Section 3.06 (c) of the Standard Conditions is three (3) years after the date of countersignature of this Agreement by the Recipient.

**Article IV**

Recipient’s Representative; Addresses

4.01. **Recipient’s Representative.** The Recipient’s Representative referred to in Section 7.02 of the Standard conditions is the Minister of Finance.

4.02. **Recipient’s Address.** The Recipient’s Address referred to in Section 7.01 of the Standard Conditions is:

- Ministry of Finance
- Tashichhodzong
- Thimphu, Kingdom of Bhutan

Cable address: Facsimile:

- Ministry of Finance
- 323154
- Thimphu, Bhutan

4.03. **World Bank’s Address.** The World Bank’s Address referred to in Section 7.01 of the Standard Conditions is:

International Bank for Reconstruction and Development
1818 H Street, N.W.
Washington, D.C. 20433
United States of America

Cable: INTBAFRAD
Telex: 248423 (MCI) or 64145 (MCI)
Facsimile: 1-202-477-6391
Appendix to the Annex

National Competitive Bidding Procedures

In order to ensure economy, efficiency and transparency and broad consistency with the provisions of Section I of the Procurement Guidelines the following should be followed:

(a) invitations to bid shall be advertised in at least one (1) widely circulated national newspaper or in the official gazette, or on a widely used website or electronic portal with free national and international access, in English, at least thirty (30) days prior to the deadline for the submission of bids;

(b) bid documents shall be made available, by mail or in person, to all who are willing to pay the required fee;

(c) evaluation of bids shall be made in strict adherence to the criteria disclosed in the bidding documents, in a format and specified period agreed with the World Bank;

(d) bids shall be opened in public in one place, immediately after the deadline for submission of bids;

(e) foreign bidders shall not be precluded from bidding and no preference of any kind shall be given to national bidders;

(f) qualification criteria (in case pre-qualifications were not carried out) shall be stated in the bidding documents, and if a registration process is required, a foreign firm declared as the lowest evaluated bidder shall be given a reasonable opportunity of registering, without let or hindrance;

(g) contracts shall be awarded to the lowest evaluated bidders;

(h) post-bidding negotiations shall not be allowed with the lowest evaluated bidders or any other bidders;

(i) bids shall not be rejected merely on the basis of a comparison with an official estimate without the prior concurrence of the World Bank;

(j) annual rate contracts entered into by the implementing entity shall not be acceptable as a substitute for National Competitive Bidding Procedure; such contracts shall be acceptable for any procurement under Shopping as one of the quotation;

(k) re-bidding shall not be carried out without the prior concurrence of the World Bank;

(l) all bidders/contractors shall provide bid/performance security as indicated in the bidding/contract documents;
(m) a bidder’s bid security shall apply only to a specific bid, and a contractor’s performance security shall apply only to the specific contract under which it was furnished;

(n) split award or lottery in award of contracts shall not be carried out when two (2) or more bidders quote the same lowest price, an investigation shall be made to determine any evidence of collusion, following which:

(i) if collusion is determined, the parties involved shall be disqualified and the award shall then be made to the next lowest evaluated and qualified bidder; and

(ii) if no evidence of collusion can be confirmed, then fresh bids shall be invited after receiving the concurrence of the World Bank;

(o) extension of bid validity shall not be allowed without the prior concurrence of the World Bank: (i) for the first request for extension if it is longer than eight (8) weeks, and (ii) for all subsequent requests for extension irrespective of the period;

(p) bids shall not be invited on the basis of percentage premium or discount over the estimated cost; and

(q) there shall not be any restrictions on the means of delivery of the bids except electronic submission of bidding documents.