



CONGRESSIONAL NOTIFICATION TRANSMITTAL SHEET

In accordance with section 610(b)(1) of the Millennium Challenge Act of 2003, as amended, we wish to inform you that the Millennium Challenge Corporation (“MCC”) entered into a Millennium Challenge Compact with the Republic of El Salvador on September 30, 2014 (the “Compact”). We have included a detailed summary of the Compact and a copy of the text of the Compact.

We will identify a link to the Compact and a summary of it in the Federal Register and on MCC’s website.

The attached notification is being sent to Congress on October 9, 2014.

Sincerely,

/s/

Paul Weinberger
Vice President
Congressional and Public Affairs

Enclosure: As stated

**MILLENNIUM CHALLENGE CORPORATION
CONGRESSIONAL NOTIFICATION**

October 9, 2014

In accordance with section 610(b)(1) of the Millennium Challenge Act of 2003, as amended (22 U.S.C. 7701 et seq.) (the “Act”), this notification is to advise that the Millennium Challenge Corporation (“MCC”) entered into a Millennium Challenge Compact with the Republic of El Salvador under section 605 of the Act on September 30, 2014 (the “Compact”).

A detailed summary of the Compact and a copy of the text of the Compact follow.

SUMMARY OF COMPACT

MILLENNIUM CHALLENGE COMPACT BETWEEN THE UNITED STATES OF AMERICA, ACTING THROUGH THE MILLENNIUM CHALLENGE CORPORATION, AND THE REPUBLIC OF EL SALVADOR

Overview

The Millennium Challenge Corporation (“MCC”) has signed a five-year, \$277 million compact with the Republic of El Salvador aimed at reducing poverty and accelerating economic growth (the “Compact”). The Compact is intended to assist the Government of El Salvador (“GoES”) to strengthen the investment climate, enhance the role of public-private partnerships in delivering key services, and improve the country’s productivity and competitiveness in international markets. Through intensive policy reforms and an integrated set of investments in the institutional capital, human capital, and physical capital of El Salvador, MCC expects that the Compact will help set the foundation for lasting economic growth and poverty reduction.

Background

This Compact will build on GoES reforms and initiatives and is informed by consultations with over 200 businesses. First, the Compact will invest in the **institutional capital** of El Salvador in order to enhance the investment climate by streamlining the regulatory environment and supporting the implementation of public-private partnerships. Second, the Compact will support policy reforms and invest in **human capital** to improve education quality and better match workforce skills with the demands of the labor market. Third, the Compact will invest in **physical capital** to reduce logistics and transportation costs by improving key road segments and border infrastructure in major transport corridors.

The Compact’s three projects represent a total investment of \$365.2 million, of which MCC will contribute \$277 million, and the GoES will commit \$88.2 million – a 32 percent matching contribution that is well above the 15 percent country contribution required for second compacts with lower-middle income countries.

Program Overview and Budget

Below is a summary describing the components of the Compact. The budget and expected impacts are preliminary based on due diligence and project appraisal.

Compact Budget Overview

| Project | MCC Funding | GoES Funding | Total Investment | Portion of Budget |
|--|------------------|-----------------|---------------------|----------------------|
| | Millions of US\$ | | | |
| Investment Climate Project | 42.4 | 50.0 | 92.4 | 25.3% |
| Human Capital Project | 100.7 | 15.0 | 115.7 | 31.7% |
| Logistical Infrastructure Project | 109.6 | 15.7 | 125.3 | 34.3% |
| Monitoring and Evaluation | 4.3 | | 4.3 | 1.2% |
| Program Administration | 20.0 | 7.5 | 27.5 | 7.5% |
| TOTAL | \$277.0 | \$88.2 | \$365.2 | 100% |

Summary of Projects and Activities

Investment Climate Project

The constraints to economic growth analysis and consultations with investors identified excessive “red tape” and discretionary application of rules as negatively affecting the investment climate in El Salvador. Firms also identified the need for key public infrastructure to increase productivity, but tight fiscal constraints and weak institutional capacity limit the ability of the GoES to provide such infrastructure. The Investment Climate Project seeks to address these deficiencies in El Salvador’s investment climate by improving the regulatory environment and the GoES’s capacity to provide key public services in partnership with the private sector through the following two activities:

- The *Regulatory Improvement Activity* will prioritize and promote investment climate reforms with the goal of creating a more efficient and profitable business environment. MCC will support the development of an institutional framework and system, including an independent institution focused on continuous regulatory improvement and the prioritization and implementation of a select set of reforms. The reforms will focus on areas critical to El Salvador’s competitiveness in international markets and may include trade facilitation, border crossing and customs procedures, environmental permitting, and harmonization of municipal and national regulations. The regulatory improvement institution will also consider the extent to which regulations can be improved to reduce the potential for corruption. In designing and implementing reforms, the institution will ensure that the proposed reforms are consistent with the GoES’s obligations under international trade and investment agreements, including the Dominican Republic-Central America Free Trade Agreement. As part of the activity, the GoES will commit to review, simplify and potentially eliminate regulations early in the Compact implementation process. Such concrete demonstrations of high level commitment to the reform process will be necessary to achieve a dramatic change in the perceptions of the business climate in El Salvador.
- The *Partnership Development Activity* seeks to enable the GoES to partner with private enterprise in innovative ways to provide critical public services in the face of tight fiscal

constraints. The GoES has recently passed several laws to facilitate private investment and trade. Most notably, the GoES legislature unanimously passed a law in May 2013 and subsequent reforms in May 2014 to facilitate public-private partnerships (“PPPs”) in the provision of key public services. MCC will invest in capacity building to properly develop, implement, and monitor such partnerships under this law. MCC will make available funding for transaction advisory services to develop and tender PPPs for two key infrastructure projects. Projects currently under review are the expansion of the El Salvador International Airport and a wind farm. MCC and the GoES are also sponsoring the El Salvador Investment Challenge (“ESIC”), a program to more efficiently and transparently allocate limited GoES resources to public goods needed to support private investment in the international trade of goods and services. The ESIC generated 74 investment project proposals in its initial call for proposals, of which 13 are being evaluated for the next phase of development. The GoES plans to institutionalize the ESIC as an instrument for attracting private investment and will contribute up to \$50 million to the ESIC during the term of the Compact.

The estimated economic rate of return (“ERR”) for the Investment Climate Project is 18.56 percent, using a weighted estimate of the calculated ERRs for each activity.

Human Capital Project

The quality of education in El Salvador is below what the country requires to be competitive in world markets. The Human Capital Project is designed to improve the quality of education and to better match the supply of skills of students coming out of secondary school with the demand of a labor market oriented towards international trade. The project consists of the following two activities:

- The *Education Quality Activity* supports complementary interventions to provide Salvadoran students the benefits of competency-based education, increased classroom time, teachers trained in requisite subject-matters and pedagogical skills, and an institutional and physical environment conducive to learning. MCC’s investment will strengthen the national education system by reforming the laws, policies, and operations that govern continuous professional development for teachers, student assessment, and information systems. The activity will strengthen and expand the implementation of the full-time inclusive school model, which increases classroom time from 25 to 40 hours per week, in an estimated 400 schools grouped in 45-55 clusters, focusing resources on grades 7-12. The curriculum improvement component will focus on English, mathematics, science and information technology, and other 21st century skills.
- The *Technical, Vocational Education and Training (“TVET”) System Reform Activity* seeks to harmonize the skills supplied by private and public TVET providers with the skills demanded by the labor market. The activity will strengthen the national TVET governance system by supporting legal, policy, and operational reforms within the system. MCC will support the establishment of a public entity governed by a board comprised of an equal number of public and private sector representatives to provide the legal and institutional framework for an integrated TVET system. The activity will also fund TVET curricula

development with participation from the private sector, career counseling, and job-matching services. It will also fund the establishment of a framework and standards for accreditation of TVET training organizations and certification of teachers and students. The activity will also strengthen the capacity of the TVET system for identifying labor market trends that will inform the strategic direction of the TVET system, including the establishment of a monitoring and evaluation (“M&E”) framework and a labor market observatory.

The estimated ERR for the Human Capital Project is 11.35 percent.

Logistical Infrastructure Project

The constraints analysis identified transportation and logistics as main factors contributing to the productivity and competitiveness of Salvadoran exports. Consultations with businesses during Compact development also highlighted certain transportation and logistics deficiencies, including the need to expand and rehabilitate key road segments in the coastal zone of El Salvador. The Logistical Infrastructure Project is comprised of two activities designed to reduce logistical and transportation costs and relieve bottlenecks at critical sections along the logistical corridor that connects the main border crossing with Honduras at El Amatillo, the Ports of La Union and Acajutla, and the international airport:

- The *Coastal Highway Expansion Activity* seeks to relieve congestion at the most transited segment (27 kilometers) of El Salvador’s coastal highway by expanding this road from two to four lanes. The coastal highway is one of the two most important logistical corridors in the country and connects the country’s major logistical nodes along the Southern coastal zone of the country, including its two sea ports (La Union and Acajutla) and the international airport.
- The *Border Crossing Infrastructure Activity* seeks to relieve the freight and passenger traffic congestion at the border crossing into Honduras at El Amatillo by improving a 5.7 kilometer road leading to the border and modernizing the border-crossing facilities on the Salvadoran side. MCC will invest in the construction of control stations at the border, including buildings, internal access and connecting roads, parking areas, water and sanitation, and other infrastructure components that may be necessary for the effective functioning of these stations.

The estimated ERR for the Logistical Infrastructure Project is 20.31 percent, using a weighted estimate of the calculated ERRs for each activity.

Program Logic, Expected Results, and Beneficiaries

In order for El Salvador to be competitive and raise productivity in internationally-traded goods and services, the factors of production in El Salvador must be competitive on world markets.

Those factors include human capital, physical capital, and often logistics/transportation. The institutional environment can also affect productivity. As a result, the Compact takes a multi-pronged approach to enhance El Salvador's competitiveness in these factors of productivity.

By streamlining the business environment, improving the quality of education, and reducing transportation and logistics costs, MCC's investments are intended to increase the productivity of current firms involved in the trade of international goods and services, which is expected to increase current production (and subsequently, employment). Firms are then expected to invest new revenues in more productive technology to realize greater returns on future production. Higher employment and output are expected over time through this self-reinforcing feedback loop which is enabled by greater productivity in traded goods and services.

The expected beneficiaries of the Regulatory Improvement Activity are the firms operating in El Salvador (currently more than 25,000) that will experience cost savings as a result of regulatory reforms. The potential expansion of the El Salvador International Airport under the Partnership Development Activity is expected to decrease delays and travel costs for travelers, while the wind farm project would increase the GoES's ability to attract investment for renewable energy. The beneficiaries of the ESIC are expected to be those firms whose proposals are selected for grant funding, workers who realize net income gains associated with employment as a result of the projects, and third parties who benefit from the public investment.

MCC expects the Human Capital Project to directly benefit students in grades 7-12 in general and technical education, who realize higher incomes as a result of more years of education. In particular, the project is expected to contribute to preventing or postponing the dropout of approximately 176,000 students. Direct beneficiaries of the TVET System Reform Activity are expected to be TVET students who receive higher incomes as a result of receiving skills that are better matched to labor market needs. Additional beneficiaries of the project include students who do not attend a full-time inclusive school but receive increased incomes as a result of improved quality of education that result from the implementation of reforms at the national level. Communities may also experience reductions in crime as a result of the full-time inclusive school model, due to increased permanence in school and lowered social vulnerability of students.

The beneficiaries for the Logistical Infrastructure Project are the estimated 171,159 individuals living within five kilometers of either side of the project sites. Because of the nature of the activities as key logistical thoroughfares, benefits in the form of reduced vehicle operating costs and travel time are expected to accrue to individuals and firms that travel along those corridors.

2006 El Salvador Compact Update and Sustainability Information

In November 2006, the Millennium Challenge Corporation signed a five-year, \$460.94 million compact (the "2006 Compact") with the GoES to improve the economic opportunities of Salvadorans through strategic investments in agricultural production, rural business development, education, and transportation infrastructure. The 2006 Compact consisted of the following three projects:

1. The Connectivity Project, to reduce travel cost and time within the Northern Zone,
2. The Human Development Project, to increase the human and physical capital of residents of the Northern Zone and further employment and business opportunities, and
3. The Productive Development Project, to increase production and employment through technical assistance, credit guarantees, and capital investments.

The 2006 Compact entered into force on September 20, 2007 and closed on September 20, 2012.

Key Achievements of the Compact are as follows:

- **Connectivity Project:** A total of 223.32 kilometers of road, including three large bridges, and 20 smaller bridges were constructed in northern El Salvador to help improve connectivity for farmers and local producers with the rest of the country. This east-west road in the north stretches close to the borders with Guatemala to the west and Honduras to the east, and the improvements have reduced travel time across the Northern Zone from 12 hours to 6.5 hours.
- **Human Development Project:**
 - Electrification: An estimated 35,412 households now have electricity in their homes, thanks to the installation of new power lines and solar power systems, helping to increase the percentage of households with electricity connections in the Northern Zone from 78 percent in 2007 to 90 percent in 2011.
 - Water and Sanitation: MCC funded about 272 kilometers of water pipes as part of the 2006 Compact's investment in water and basic sanitation that helped connect 7,624 households to potable water.
 - Education: MCC funded the construction of a new technical community college, improvements to a teacher training center, and the expansion and rehabilitation of 20 high schools. The rehabilitation of the high schools alone is expected to benefit more than 9,700 students every year.
- **Productive Development Project:** MCC funding assisted an estimated 17,500 producers through the provision of training, seeds, equipment, and technical assistance. The project provided 30 loans to small and medium-sized businesses in the Northern Zone to develop new or expand investments in the agriculture, tourism and handicrafts value chains. These loans totaled \$5.7 million, of which approximately 20 percent went to women-owned businesses.

Sustainability:

Although no contribution was required from El Salvador during the implementation of the 2006 Compact, the GoES contributed substantially in parallel to the Compact to enhance the success of the program.

The **Connectivity Project:** In the final year of compact implementation (2012), the GoES also carried out two road maintenance reforms, increasing annual road maintenance funding by about

\$26 million (~37% increase). At the end of the five years, the GoES allocated an additional \$13 million to complete two remaining segments of the Northern Transnational Highway. During the four-month closure period, all activities under the 2006 Compact were successfully completed.

The **Human Development Project's** activities were extensions of existing GoES programs, built on the National Plan for Education 2021 and designed to strengthen and install permanent capacities in key Salvadoran ministries and institutions. In addition, the Ministry of Education agreed to fund infrastructure and equipment maintenance and continued an agreement with the Gloria de Kriete Foundation to fund scholarship for secondary education through 2014.

The **Productive Development Project** was designed to transition producers to higher-profit activities, generate new investment, expand markets and sales, and create new jobs in ways that stimulate sustainable economic growth and poverty reduction. Actions accomplished to ensure sustainability of investments made under the Productive Development Project included the establishment of contracts between beneficiaries and supported cooperatives and major retailers for the purchase of horticulture and dairy products. The Ministry of Agriculture also incorporated the project's beneficiaries into its national Family Agriculture Plan, its signature agriculture extension service aimed at improving the profitability of individual and small and medium-sized producers.

Environmental and Social Sustainability:

As part of an effort to ensure environmental and social sustainability, all Projects included consultations with the public regarding various aspects of their implementation. The design of the Projects, including their major activities, was included in a strategic environmental assessment that was completed prior to implementation. The sustainability of the projects was also enhanced by the institutional capacity building and training in environmental management acquired through the close cooperation among the environmental units of the implementing agencies, the Millennium Challenge Account (MCA), and MCC. The Salvadoran Ministry of Environment (MARN) received Compact funding support to offset the additional regulatory costs associated with the Projects. Over the course of the Compact, collaboration improved between MARN and the environment units of the implementing agencies.

The GoES and private sector and civil society organizations have consistently worked to ensure the sustainability of the 2006 Compact and we expect them to continue to support these investments going forward.

MILLENNIUM CHALLENGE COMPACT

BETWEEN

THE UNITED STATES OF AMERICA

ACTING THROUGH

THE MILLENNIUM CHALLENGE CORPORATION

AND

THE REPUBLIC OF EL SALVADOR

ACTING THROUGH

THE MINISTRY OF FOREIGN AFFAIRS

MILLENNIUM CHALLENGE COMPACT
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Annex I: Program Description

Annex II: Multi-Year Financial Plan Summary

Annex III: Compact Monitoring & Evaluation Summary

Annex IV: Conditions Precedent to Disbursement of Compact Implementation Funding

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MILLENNIUM CHALLENGE COMPACT

PREAMBLE

This MILLENNIUM CHALLENGE COMPACT (this “*Compact*”) is between the United States of America, acting through the Millennium Challenge Corporation, a United States government corporation (“*MCC*”), and the Republic of El Salvador (“*El Salvador*”), acting through the Ministry of Foreign Affairs (the “*Government*”) (individually a “*Party*” and collectively, the “*Parties*”). Capitalized terms used in this Compact will have the meanings provided in Annex V.

Recalling that the Parties successfully concluded an initial Millennium Challenge Compact that advanced the progress of El Salvador in achieving lasting economic growth and poverty reduction, demonstrated the strong partnership between the Parties, and was implemented in accordance with MCC’s core policies and standards;

Recognizing that the Parties are committed to the shared goals of promoting economic growth and the elimination of extreme poverty in El Salvador and that MCC assistance under this Compact supports El Salvador’s demonstrated commitment to strengthening good governance, economic freedom and investments in people;

Recalling that the Government consulted with the private sector and civil society of El Salvador to determine the priorities for the use of MCC assistance and developed and submitted to MCC a proposal for such assistance to achieve lasting economic growth and poverty reduction; and

Recognizing that MCC wishes to help El Salvador implement the program described herein to achieve the goal and objectives described herein (as such program description and objectives may be amended from time to time in accordance with the terms hereof, the “*Program*”);

The Parties hereby agree as follows:

ARTICLE 1.

GOAL AND OBJECTIVES

Section 1.1 Compact Goal. The goal of this Compact is to reduce poverty through economic growth in El Salvador (the “*Compact Goal*”). MCC’s assistance will be provided in a manner that strengthens good governance, economic freedom, and investments in the people of El Salvador.

Section 1.2 Program Objective. The objective of the Program (the “*Program Objective*”) is to increase El Salvador’s productivity and competitiveness in international markets. The Program consists of the projects described in Annex I (each a “*Project*” and collectively, the “*Projects*”).

Section 1.3 Project Objectives. The objective of each of the Projects (each a “*Project Objective*” and collectively, the “*Project Objectives*”) is to:

- (a) increase private investment by improving El Salvador’s regulatory environment and institutional capacity and providing key public services in partnership with the private sector;
- (b) improve the quality of education and better match the skills demanded by employers in the international trade of goods and services, thus increasing the labor productivity of future Salvadoran workers; and
- (c) reduce logistical and transportation costs to increase investment and productivity in the trade of goods and services.

ARTICLE 2.
FUNDING AND RESOURCES

Section 2.1 Program Funding.

Upon entry into force of this Compact in accordance with Section 7.3, MCC will grant to the Government, under the terms of this Compact, an amount not to exceed Two Hundred Sixty Seven Million United States Dollars (US\$267,000,000) (“**Program Funding**”) for use by the Government to implement the Program. The multi-year budget allocation of Program Funding is generally described in Annex II.

Section 2.2 Compact Implementation Funding.

(a) Upon the provisional application of this Compact in accordance with Section 7.5, MCC will grant to the Government, under the terms of this Compact and in addition to the Program Funding described in Section 2.1, an amount not to exceed Ten Million United States Dollars (US\$10,000,000) (“**Compact Implementation Funding**”) under Section 609(g) of the Millennium Challenge Act of 2003, as amended (the “**MCA Act**”), for use by the Government to facilitate implementation of the Compact, including for the following purposes:

- (i) financial management and procurement activities (including costs related to agents procured by MCC to provide standby fiscal and procurement agent services, if required);
- (ii) administrative activities (including start-up costs such as staff salaries) and administrative support expenses such as rent, computers and other information technology or capital equipment;
- (iii) monitoring and evaluation activities;
- (iv) feasibility, design and other project preparatory studies (including the Road Maintenance Study, as defined in Annex I hereto); and
- (v) other activities to facilitate Compact implementation as approved by MCC.

The multi-year budget allocation of Compact Implementation Funding is generally described in Annex II.

(b) In accordance with Section 7.5, this Section 2.2 and other provisions of this Compact applicable to Compact Implementation Funding will be effective, for purposes of Compact Implementation Funding only, as of the date this Compact is signed by MCC and the Government.

(c) Each Disbursement of Compact Implementation Funding is subject to satisfaction of the conditions precedent to such disbursement as set forth in Annex IV.

(d) If MCC determines that the full amount of Compact Implementation Funding available under Section 2.2(a) exceeds the amount that reasonably can be utilized for the purposes set forth in Section 2.2(a), MCC, by written notice to the Government, may withdraw the excess amount, thereby reducing the amount of the Compact Implementation Funding available under Section 2.2(a) (such excess, the “**Excess CIF Amount**”). In such event, the amount of Compact Implementation Funding granted to the Government under Section 2.2(a) will be reduced by the Excess CIF Amount, and MCC will have no further obligations with respect to such Excess CIF Amount.

(e) MCC, at its option by written notice to the Government, may elect to grant to the Government an amount equal to all or a portion of such Excess CIF Amount as an increase in the Program Funding, and such additional Program Funding will be subject to the terms and conditions of this Compact applicable to Program Funding.

Section 2.3 MCC Funding.

Program Funding and Compact Implementation Funding are collectively referred to in this Compact as “**MCC Funding**,” and includes any refunds or reimbursements of Program Funding or Compact Implementation Funding paid by the Government in accordance with this Compact.

Section 2.4 Disbursement.

In accordance with this Compact and the Program Implementation Agreement, MCC will disburse MCC Funding for expenditures incurred in furtherance of the Program (each instance, a “**Disbursement**”). Subject to the satisfaction of all applicable conditions precedent, the proceeds of Disbursements will be made available to the Government, at MCC’s sole election, by (a) deposit to one or more bank accounts established by the Government and acceptable to MCC (each, a “**Permitted Account**”) or (b) direct payment to the relevant provider of goods, works or services for the implementation of the Program. MCC Funding may be expended only for Program expenditures.

Section 2.5 Interest. The Government will pay or transfer to MCC, in accordance with the Program Implementation Agreement, any interest or other earnings that accrue on MCC Funding prior to such funding being used for a Program purpose.

Section 2.6 Government Resources; Budget.

(a) In accordance with Section 609(b)(2) of the MCA Act, the Government will make a contribution towards meeting the Program Objective and Project Objectives of this Compact, and such contribution will be equal to at least fifteen percent (15%) of the total amount of MCC Funding. Annex II describes such contribution in more detail. In addition, the Government will

provide all funds and other resources, and will take all actions, that are necessary to carry out the Government's responsibilities under this Compact.

(b) The Government will use its best efforts to ensure that all MCC Funding it receives or is projected to receive in each of its fiscal years is fully reported in the Government's financial management report (*Informe de Gestión Financiera del Estado*) for the duration of the Program.

(c) The Government will not reduce the normal and expected resources that it would otherwise receive or budget from sources other than MCC for the activities contemplated under this Compact and the Program.

(d) Unless the Government discloses otherwise to MCC in writing, MCC Funding will be in addition to the resources that the Government would otherwise receive or budget for the activities contemplated under this Compact and the Program.

Section 2.7 Limitations on the Use of MCC Funding. The Government will ensure that MCC Funding is not used for any purpose that would violate United States law or policy, as specified in this Compact or as further notified to the Government in writing or by posting from time to time on the MCC website at www.mcc.gov (the "*MCC Website*"), including but not limited to the following purposes:

(a) for assistance to, or training of, the military, police, militia, national guard or other quasi-military organization or unit;

(b) for any activity that is likely to cause a substantial loss of United States jobs or a substantial displacement of United States production;

(c) to undertake, fund or otherwise support any activity that is likely to cause a significant environmental, health, or safety hazard, as further described in MCC's *Environmental Guidelines* and any guidance documents issued in connection with the guidelines posted from time to time on the MCC Website or otherwise made available to the Government (collectively, the "*MCC Environmental Guidelines*"); or

(d) to pay for the performance of abortions as a method of family planning or to motivate or coerce any person to practice abortions, to pay for the performance of involuntary sterilizations as a method of family planning or to coerce or provide any financial incentive to any person to undergo sterilizations or to pay for any biomedical research which relates, in whole or in part, to methods of, or the performance of, abortions or involuntary sterilization as a means of family planning.

Section 2.8 Taxes.

(a) Unless the Parties specifically agree otherwise in writing, the Government will ensure that all MCC Funding and the Government Contribution, as defined in Annex II, is free from the payment or imposition of any existing or future taxes, duties, levies, special contributions or other similar charges (but not fees or charges for services that are generally applicable in El Salvador, reasonable in amount and imposed on a non-discriminatory basis) ("*Taxes*") of or in El Salvador (including any such Taxes imposed by a national, regional, municipal, local or other governmental or taxing authority of or in El Salvador). Specifically,

and without limiting the generality of the foregoing, MCC Funding will be exempt from the payment of (i) any tariffs, customs duties, import taxes (including VAT), export taxes, and other similar charges on any goods, works or services introduced into El Salvador in connection with the Program; (ii) sales tax, value added tax, excise tax, property transfer tax, withholding or tax collection, and other similar charges on any transactions involving goods works or services in connection with the Program, as well as any other tax, duty, encumbrance or extraordinary tax on transfers or financial transactions to El Salvador or within its Territory; (iii) taxes and other similar charges on ownership, possession or use of any property, patrimony or assets in connection with the Program; (iv) taxes, withholding taxes, and other similar charges on income, profits or gross receipts attributable to work performed in connection with the Program (none of which shall be considered income, profits, receipts or revenues upon receipt of payment or transfer of MCC Funding or the Government Contribution hereunder in furtherance of the Compact and therefore are excluded from the definition of income) and related social security taxes and other similar charges on all natural or legal persons performing work in connection with the Program; and (v) special contributions or additional charges for fuel or gasoline, and on vehicle registration and circulation permits. The exemption hereunder for Taxes also includes (A) taxes, including municipal taxes; and (B) special contributions that do not bear a reasonable relationship to the cost of a service being provided, either of which levied by any municipality.

(b) The mechanisms that the Government will use to implement the principal tax exemptions required by Section 2.8(a) will be set forth in the Program Implementation Agreement. Such mechanisms may include exemptions from the payment of Taxes that have been granted in accordance with applicable law, refund or reimbursement of Taxes by the Government to MCC, MCA-El Salvador or to the taxpayer, or payment by the Government to MCA-El Salvador or MCC, for the benefit of the Program, of an agreed amount representing any collectible Taxes on the items described in Section 2.8(a).

(c) If a Tax has been paid contrary to the requirements of Section 2.8(a) or the Program Implementation Agreement, the Government will refund promptly to MCC (or to another party as designated by MCC) the amount of such Tax in United States dollars or the currency of El Salvador within thirty (30) days (or such other period as may be agreed in writing by the Parties) after the Government is notified in writing (whether by MCC or MCA-El Salvador) that such Tax has been paid.

(d) No MCC Funding, proceeds thereof or Program Assets may be applied by the Government in satisfaction of its obligations under Section 2.8(c).

Section 2.9 Lower Middle Income Countries. Section 606(b) of the MCA Act restricts the amount of assistance that MCC may provide to “lower middle income countries,” a term that is defined in the MCA Act and includes El Salvador. To the extent that MCC determines, in MCC’s reasonable discretion, that the amount of Program Funding granted to the Government in this Compact might exceed the limit stipulated in Section 606(b) of the MCA Act, MCC, at any time and from time to time upon written notice to the Government, may reduce the amount of Program Funding, or withhold any Disbursement of Program Funding. In such event, the Parties will use their best efforts to determine the optimal allocation of MCC Funding, as modified consistent with this Section 2.9, to address existing liabilities incurred in furtherance of this Compact.

ARTICLE 3.
IMPLEMENTATION

Section 3.1 Program Implementation Agreement. The Parties will enter into an agreement providing further detail on the implementation arrangements, fiscal accountability and disbursement and use of MCC Funding, among other matters (the “***Program Implementation Agreement***” or “***PIA***”); and the Government will implement the Program in accordance with this Compact, the PIA, any other Supplemental Agreement and any Implementation Letter.

Section 3.2 Government Responsibilities.

(a) The Government has principal responsibility for overseeing and managing the implementation of the Program.

(b) (i) With the prior written consent of MCC, the Government will designate an entity to be established by law as an autonomous entity of public nature and utility, as the accountable entity to implement the Program and to exercise and perform the Government’s right and obligation to oversee, manage and implement the Program, including without limitation, managing the implementation of Projects and their Activities, allocating resources and managing procurements. Such entity will be referred to herein as “***MCA-El Salvador***” or “***FOMILENIO II.***” MCA-El Salvador will have the authority to bind the Government with regard to all Program activities. The designation contemplated by this Section 3.2(b)(i) will not relieve the Government of any obligations or responsibilities hereunder or under any related agreement, for which the Government remains fully responsible. MCC hereby acknowledges and consents to the designation in this Section 3.2(b)(i).

(ii) The patrimony of MCA-El Salvador will be constituted through the grant of MCC Funding and the Government Contribution pursuant to this Compact. MCA-El Salvador will have a multi-annual budget that will be approved as an extraordinary budget by the *Asamblea Legislativa* of El Salvador.

(c) The Government will ensure that any Program Assets or services funded in whole or in part (directly or indirectly) by MCC Funding are used solely in furtherance of this Compact and the Program unless MCC agrees otherwise in writing.

(d) The Government will take all necessary or appropriate steps to achieve the Program Objective and the Project Objectives during the Compact Term (including, without limiting Section 2.6(a), funding all costs that exceed MCC Funding and are required to carry out the terms hereof and achieve such objectives, unless MCC agrees otherwise in writing).

(e) The Government will ensure that the Program is implemented and that the Government carries out its obligations hereunder with due care, efficiency and diligence in conformity with sound technical, financial, and management practices, and in conformity with this Compact, the Program Implementation Agreement, any other Supplemental Agreement and the Program Guidelines.

(f) The Government grants to MCC a perpetual, irrevocable, royalty-free, worldwide, fully paid, assignable right and license to practice or have practiced on its behalf (including the right to produce, reproduce, publish, repurpose, use, store, modify, or make available) any

portion or portions of Intellectual Property as MCC sees fit in any medium, now known or hereafter developed, for any purpose whatsoever.

Section 3.3 Policy Performance. In addition to undertaking the specific policy, legal and regulatory reform commitments identified in Annex I (if any), the Government will seek to maintain and to improve its level of performance under the policy criteria identified in Section 607 of the MCA Act, and the selection criteria and methodology used by MCC.

Section 3.4 Accuracy of Information. The Government assures MCC that, as of the date this Compact is signed by the Government, the information provided to MCC by or on behalf of the Government in the course of reaching agreement with MCC on this Compact is true, correct and complete in all material respects.

Section 3.5 Implementation Letters. From time to time, MCC may provide guidance to the Government in writing on any matters relating to this Compact, MCC Funding or implementation of the Program (each, an “**Implementation Letter**”). The Government will use such guidance in implementing the Program.

Section 3.6 Procurement and Grants.

(a) The Government will ensure that the procurement of all goods, works and services by the Government or any Provider to implement the Program will be in accordance with the MCC *Program Procurement Guidelines* posted from time to time on the MCC Website (the “**MCC Program Procurement Guidelines**”). Accordingly, neither the *Ley de Adquisiciones y Contrataciones de la Administración Pública*, its corresponding Executive Decree or any other laws or regulations of the Republic of El Salvador regarding procurements will apply thereto. The MCC Program Procurement Guidelines include the following requirements, among others:

(i) open, fair, and competitive procedures must be used in a transparent manner to solicit, award and administer contracts and to procure goods, works and services;

(ii) solicitations for goods, works, and services must be based upon a clear and accurate description of the goods, works and services to be acquired;

(iii) contracts must be awarded only to qualified contractors that have the capability and willingness to perform the contracts in accordance with their terms on a cost effective and timely basis; and

(iv) no more than a commercially reasonable price, as determined, for example, by a comparison of price quotations and market prices, will be paid to procure goods, works and services.

(b) Unless MCC otherwise consents in writing, the Government will ensure that any grant issued in furtherance of the Program (each, a “**Grant**”) is awarded, implemented and managed pursuant to open, fair and competitive procedures administered in a transparent manner acceptable to MCC. In furtherance of this requirement, and prior to the issuance of any Grant, the Government and MCC will agree upon written procedures to govern the identification of potential Grant recipients, including, without limitation, appropriate eligibility and selection criteria and award procedures. Such agreed procedures will be posted on the MCA-El Salvador website.

Section 3.7 Records; Accounting; Covered Providers; Access.

(a) Government Books and Records. The Government will maintain, and will use its best efforts to ensure that all Covered Providers maintain, accounting books, records, documents and other evidence relating to the Program adequate to show, to MCC's satisfaction, the use of all MCC Funding and the implementation and results of the Program ("**Compact Records**"). In addition, the Government will furnish or cause to be furnished to MCC, upon its request, originals or copies of such Compact Records.

(b) Accounting. The Government will maintain and will use its best efforts to ensure that all Covered Providers maintain Compact Records in accordance with generally accepted accounting principles prevailing in the United States, or at the Government's option and with MCC's prior written approval, other accounting principles, such as those (i) prescribed by the International Accounting Standards Board, or (ii) then prevailing in El Salvador. Compact Records must be maintained for at least five (5) years after the end of the Compact Term or for such longer period, if any, required to resolve any litigation, claims or audit findings or any applicable legal requirements.

(c) Access. Upon MCC's request, the Government, at all reasonable times, will permit, or cause to be permitted, authorized representatives of MCC, the Inspector General of MCC ("**Inspector General**"), the United States Government Accountability Office, any auditor responsible for an audit contemplated herein or otherwise conducted in furtherance of this Compact, and any agents or representatives engaged by MCC or the Government to conduct any assessment, review or evaluation of the Program, the opportunity to audit, review, evaluate or inspect facilities, assets and activities funded in whole or in part by MCC Funding.

Section 3.8 Audits; Reviews.

(a) Government Audits. Except as the Parties may agree otherwise in writing, the Government will, on an annual basis (or on a more frequent basis if requested by MCC in writing), conduct, or cause to be conducted, financial audits of all disbursements of MCC Funding covering the period from signing of this Compact until the following December 31 and covering each twelve-month period thereafter ending December 31, through the end of the Compact Term. In addition, upon MCC's request, the Government will ensure that such audits are conducted by an independent auditor approved by MCC and named on the list of local auditors approved by the Inspector General or a United States-based certified public accounting firm selected in accordance with the *Guidelines for Financial Audits Contracted by the Millennium Challenge Corporation's Accountable Entities* (the "**Audit Guidelines**") issued and revised from time to time by the Inspector General, which are posted on the MCC Website. Audits will be performed in accordance with the Audit Guidelines and be subject to quality assurance oversight by the Inspector General. Each audit must be completed and the audit report delivered to MCC no later than 90 days after the applicable audit period, or such other period as the Parties may otherwise agree in writing.

(b) Audits of Other Entities. The Government will ensure that MCC financed agreements between the Government or any Provider, on the one hand, and (i) a United States nonprofit organization, on the other hand, state that the United States nonprofit organization is subject to the applicable audit requirements contained in OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, issued by the United States Office of

Management and Budget; (ii) a United States for-profit Covered Provider, on the other hand, state that the United States for-profit organization is subject to audit by the applicable United States Government agency, unless the Government and MCC agree otherwise in writing; and (iii) a non-US Covered Provider, on the other hand, state that the non-US Covered Provider is subject to audit in accordance with the Audit Guidelines.

(c) Corrective Actions. The Government will use its best efforts to ensure that each Covered Provider (i) takes, where necessary, appropriate and timely corrective actions in response to audits, (ii) considers whether the results of the Covered Provider's audit necessitates adjustment of the Government's records, and (iii) permits independent auditors to have access to its records and financial statements as necessary.

(d) Audit by MCC. MCC will have the right to arrange for audits of the Government's use of MCC Funding.

(e) Cost of Audits, Reviews or Evaluations. MCC Funding may be used to fund the costs of any audits, reviews or evaluations required under this Compact.

Section 3.9 Applicability of Program Guidelines. MCA-El Salvador will be subject to the accounting rules and procedures set forth in this Compact, the Program Implementation Agreement and the Program Guidelines, and will not be subject to the *Ley Organica de Administración Financiera del Estado* and *Sistema Administración Financiera Integrado*.

ARTICLE 4. COMMUNICATIONS

Section 4.1 Communications. Any document or communication required or submitted by either Party to the other under this Compact must be in writing and, except as otherwise agreed with MCC, in English; provided, however, that any amendment signed in accordance with Section 6.2(a) shall be in both English and Spanish. All such documents or communication must be submitted to the address of each Party set forth below or to such other address as may be designated by any Party in a written notice to the other Party.

To MCC:

Millennium Challenge Corporation
Attention: Vice President, Compact Operations
(with a copy to the Vice President and General Counsel)
875 Fifteenth Street, N.W.
Washington, DC 20005
United States of America
Facsimile: (202) 521-3700
Telephone: (202) 521-3600
Email: VPOperations@mcc.gov (Vice President, Compact Operations)
VPGeneralCounsel@mcc.gov (Vice President and General Counsel)

To the Government:

The Government of the Republic of El Salvador
Attention: Secretaría Técnica y de Planificación de la Presidencia
Casa Presidencial
Alameda Manuel Enrique Araujo #5500
San Salvador
Republic of El Salvador
Facsimile: (503) 2243-9943
Phone: (503) 2248-9250

Section 4.2 Representatives. For all purposes of this Compact, the Government will be represented by the individual holding the position of, or acting as, Technical and Planning Secretary of the President of the Republic of El Salvador, and MCC will be represented by the individual holding the position of, or acting as, Vice President, Compact Operations (each of the foregoing, a “**Principal Representative**”). Each Party, by written notice to the other Party, may designate one or more additional representatives (each, an “**Additional Representative**”) for all purposes of this Compact except Section 6.2(a). Once MCA-El Salvador is created and the Executive Director thereof is appointed, such Executive Director will be an Additional Representative of the Government. MCC hereby designates the Deputy Vice President, Department of Compact Operations, Europe, Asia Pacific, Latin America (EAPLA) as an Additional Representative. A Party may change its Principal Representative to a new representative that holds a position of equal or higher authority upon written notice to the other Party.

Section 4.3 Signatures. Signatures to this Compact and to any amendment to this Compact will be original signatures appearing on the same page or in an exchange of letters or diplomatic notes. With respect to all documents arising out of this Compact (other than the Program Implementation Agreement and any other legally binding international agreement) and amendments thereto, signatures may be delivered by facsimile or electronic mail and in counterparts and will be binding on the Party delivering such signature to the same extent as an original signature would be.

ARTICLE 5.

TERMINATION; SUSPENSION; EXPIRATION

Section 5.1 Termination; Suspension.

(a) Either Party may terminate this Compact without cause in its entirety by giving the other Party thirty (30) days’ prior written notice. MCC may also terminate this Compact or MCC Funding without cause in part by giving the Government thirty (30) days’ prior written notice.

(b) MCC may, immediately, upon written notice to the Government, suspend or terminate this Compact or MCC Funding, in whole or in part, and any obligation related thereto, if MCC determines that any circumstance identified by MCC, as a basis for suspension or

termination (as notified in writing to the Government) has occurred, which circumstances include but are not limited to the following:

(i) the Government fails to comply with its obligations under this Compact or any other agreement or arrangement entered into by the Government in connection with this Compact or the Program;

(ii) an event or series of events has occurred that makes it probable that the Program Objective or any of the Project Objectives will not be achieved during the Compact Term or that the Government will not be able to perform its obligations under this Compact;

(iii) a use of MCC Funding or continued implementation of this Compact or the Program violates applicable law or United States Government policy, whether now or hereafter in effect;

(iv) the Government or any other person or entity receiving MCC Funding or using Program Assets is engaged in activities that are contrary to the national security interests of the United States;

(v) an act has been committed or an omission or an event has occurred that would render El Salvador ineligible to receive United States economic assistance under Part I of the Foreign Assistance Act of 1961, as amended (22 U.S.C. 2151 *et seq.*), by reason of the application of any provision of such act or any other provision of law;

(vi) the Government has engaged in a pattern of actions inconsistent with the criteria used to determine the eligibility of El Salvador for assistance under the MCA Act; or

(vii) the Government or another person or entity receiving MCC Funding or using Program Assets is found to have been convicted of a narcotics offense or to have been engaged in drug trafficking.

Section 5.2 Consequences of Termination, Suspension or Expiration.

(a) Upon the suspension or termination, in whole or in part, of this Compact or any MCC Funding, or upon the expiration of this Compact, the provisions of Section 4.2 of the Program Implementation Agreement will govern the post-suspension, post-termination or post-expiration treatment of MCC Funding, any related Disbursements and Program Assets. Any portion of this Compact, MCC Funding, the Program Implementation Agreement or any other Supplemental Agreement that is not suspended or terminated will remain in full force and effect.

(b) MCC may reinstate any suspended or terminated MCC Funding under this Compact if MCC determines that the Government or other relevant person or entity has committed to correct each condition for which MCC Funding was suspended or terminated.

Section 5.3 Refunds; Violation.

(a) If any MCC Funding, any interest or earnings thereon, or any Program Asset is used for any purpose in violation of the terms of this Compact, then MCC may require the Government to repay to MCC in United States Dollars the value of the misused MCC Funding, interest, earnings, or asset, plus interest within thirty (30) days after the Government's receipt of

MCC's request for repayment. The Government will not use MCC Funding, proceeds thereof or Program Assets to make such payment.

(b) Notwithstanding any other provision in this Compact or any other agreement to the contrary, MCC's right under Section 5.3(a) to obtain a refund will continue during the Compact Term and for a period of (i) five (5) years thereafter or (ii) one (1) year after MCC receives actual knowledge of such violation, whichever is later.

Section 5.4 Late Payment Interest. If the Government fails to pay any amount under this Compact or the Program Implementation Agreement when due (including amounts under Section 2.8(c) and 5.3(a)), interest will be paid on such unpaid amount. Interest will accrue on such past due amount at a rate of the then current US Treasury Current Value of Funds Rate, calculated on a daily basis and a 360-day year from the due date of such payment until such amount is repaid in full. Any such repayment will first be credited against interest due, and once the interest due amount is extinguished, then repayments will be credited against outstanding principal.

Section 5.5 Survival. The Government's responsibilities under this Section 5.5 and Sections 2.7, 2.8, 3.2(f), 3.7, 3.8, 5.2, 5.3, 5.4 and 6.4 will survive the expiration, suspension or termination of this Compact.

ARTICLE 6.

COMPACT ANNEXES; AMENDMENTS; GOVERNING LAW

Section 6.1 Annexes. Each annex to this Compact constitutes an integral part hereof, and references to "Annex" mean an annex to this Compact unless otherwise expressly stated.

Section 6.2 Amendments and Modifications.

(a) The Parties may amend this Compact only by a written agreement. Such written agreement will specify how it enters into force. The Additional Representatives will not represent the Parties for such purposes.

(b) Notwithstanding Section 6.2(a), the Parties may modify any Annex, by written agreement signed by the Parties which will enter into force upon signature, to (i) suspend, terminate or modify any Project or Activity, (ii) change the allocations of funds as set forth in Annex II as of the date hereof, (iii) modify the implementation framework described in Annex I, (iv) add, change or delete any indicator, baseline or target or other information set forth in Annex II as of the date hereof, subject to and in accordance with the MCC M&E Policy, or (v) add, delete or waive any condition precedent described in Annex IV; *provided that*, in each case, any such modification (A) is consistent in all material respects with the Program Objective and Project Objectives, (B) does not cause the amount of Program Funding to exceed the aggregate amount specified in Section 2.1 (as may be modified by operation of Section 2.2(e)), (C) does not cause the amount of Compact Implementation Funding to exceed the aggregate amount specified in Section 2.2(a), (D) does not reduce the Government's responsibilities or contribution of resources required under Section 2.6(a), and (E) does not extend the Compact Term.

Section 6.3 Inconsistencies. In the event of any conflict or inconsistency between:

(a) any Annex and any of Articles 1 through 7, such Articles 1 through 7, as applicable, will prevail; or

(b) this Compact and any other agreement between the Parties regarding the Program, this Compact will prevail.

Section 6.4 Governing Law. This Compact is an international agreement and as such will be governed by the principles of international law.

Section 6.5 Additional Instruments. Any reference to activities, obligations or rights undertaken or existing under or in furtherance of this Compact or similar language will include activities, obligations and rights undertaken by, or existing under or in furtherance of any agreement, document or instrument related to this Compact and the Program.

Section 6.6 References to MCC Website. Any reference in this Compact, the PIA or any other agreement entered into in connection with this Compact, to a document or information available on, or notified by posting on the MCC Website will be deemed a reference to such document or information as updated or substituted on the MCC Website from time to time.

Section 6.7 References to Laws, Regulations, Policies and Guidelines. Each reference in this Compact, the PIA or any other agreement entered into in connection with this Compact, to a law, regulation, policy, guideline or similar document will be construed as a reference to such law, regulation, policy, guideline or similar document as it may, from time to time, be amended, revised, replaced, or extended and will include any law, regulation, policy, guideline or similar document issued under or otherwise applicable or related to such law, regulation, policy, guideline or similar document.

Section 6.8 MCC Status. MCC is a United States government corporation acting on behalf of the United States Government in the implementation of this Compact. MCC and the United States Government assume no liability for any claims or loss arising out of activities or omissions under this Compact. The Government waives any and all claims against MCC or the United States Government or any current or former officer or employee of MCC or the United States Government for all loss, damage, injury, or death arising out of activities or omissions under this Compact, and agrees that it will not bring any claim or legal proceeding of any kind against any of the above entities or persons for any such loss, damage, injury, or death. The Government agrees that MCC and the United States Government or any current or former officer or employee of MCC or the United States Government will be immune from the jurisdiction of all courts and tribunals of El Salvador for any claim or loss arising out of activities or omissions under this Compact.

Section 6.9 Consultation. Either Party may, at any time, request consultations relating to the interpretation or implementation of this Compact. Such consultations shall begin at the earliest possible date. The Parties shall enter any such consultations guided by the principle of achieving the Compact Goal in a timely and cost-effective manner. Any dispute arising under or related to this Compact shall be determined exclusively through the consultation mechanism set forth in this Section 6.9.

ARTICLE 7.
ENTRY INTO FORCE

Section 7.1 Domestic Requirements. The Government will proceed in a timely manner to complete all of its domestic requirements for this Compact to enter into force and be fully enforceable under the laws of El Salvador.

Section 7.2 Conditions Precedent to Entry into Force. Before this Compact enters into force:

(a) the Program Implementation Agreement must have been signed by the parties thereto;

(b) The Government must have delivered to MCC:

(i) a letter signed and dated by the Principal Representative of the Government, or such other duly authorized representative of the Government acceptable to MCC, confirming that the Government has completed its domestic requirements necessary for this Compact to enter into force and that the other conditions precedent to entry into force in this Section 7.2 have been met;

(ii) a signed legal opinion from the Attorney General of El Salvador (or such other legal counsel of the Government acceptable to MCC), in form and substance satisfactory to MCC; and

(iii) complete, certified copies of all decrees, legislation, regulations or other governmental documents relating to the Government's domestic requirements necessary for this Compact and the PIA to enter into force, which MCC may post on its website or otherwise make publicly available; and

(c) MCC will not have determined that after signature of this Compact, the Government has engaged in a pattern of actions inconsistent with the eligibility criteria for MCC Funding.

Section 7.3 Date of Entry into Force. This Compact will enter into force on the date of the last letter in an exchange of letters between MCC and the Government confirming that each Party has completed its domestic requirements for entry into force of this Compact and that the conditions precedent to entry into force in Section 7.2 have been met.

Section 7.4 Compact Term. This Compact will remain in force for five (5) years after its entry into force, unless terminated earlier under Section 5.1 (the "**Compact Term**").

Section 7.5 Provisional Application. Until this Compact has entered into force in accordance with Section 7.3, the Parties will provisionally apply the terms of this Compact from the date of a letter from the Government informing MCC that the Government is prepared to provisionally apply the Compact; *provided that*, no MCC Funding, other than Compact Implementation Funding, will be made available or disbursed before this Compact enters into force.

SIGNATURE PAGE FOLLOWS ON THE NEXT PAGE

Done at El Salvador, this 30 day of September 2014, in the English and Spanish languages.

FOR THE UNITED STATES OF
AMERICA, ACTING THROUGH THE
MILLENNIUM CHALLENGE
CORPORATION

FOR THE REPUBLIC OF EL SALVADOR,
ACTING THROUGH THE MINISTRY OF
FOREIGN AFFAIRS

/s/

/s/

Name: Kamran M. Khan
Title: Vice President, Compact Operations

Name: Hugo Roger Martínez Bonilla
Title: Minister of Foreign Affairs

**SIGNATURE PAGE TO MILLENNIUM CHALLENGE COMPACT
BETWEEN THE UNITED STATES OF AMERICA
ACTING THROUGH THE MILLENNIUM CHALLENGE CORPORATION
AND THE REPUBLIC OF EL SALVADOR
ACTING THROUGH THE MINISTRY OF FOREIGN AFFAIRS**

ANNEX I

PROGRAM DESCRIPTION

This Annex I describes the Program that MCC Funding and the Government Contribution (as defined in Annex II) will support in El Salvador during the Compact Term.

A. PROGRAM OVERVIEW

1. Background and Consultative Process.

(a) Background.

El Salvador is a close partner of the United States and has demonstrated a strong commitment to MCC's principles of ruling justly, investing in people, and encouraging economic freedom since emerging from a decade of civil war in 1992. As the first lower-middle income country to sign a compact with MCC in 2006, El Salvador continues to perform well on the eligibility criteria, passing thirteen (13) of twenty (20) indicators on its 2013 scorecard. In September 2012, the Government and MCC successfully completed a US\$461 million first compact focused on the economic development of the northern zone of El Salvador. Recognizing El Salvador's commitment to broad-based economic growth, poverty reduction, democracy, and human rights, the United States selected El Salvador as one of only four countries to participate in the Partnership for Growth ("*PfG*"), a USG whole-of-government effort to put into practice the principles of President Obama's Presidential Policy Directive on Global Development.

As a small country, El Salvador has pursued a development strategy based on a market economy, open to trade and foreign investment. It adopted the United States Dollar as its currency in 2001 and ratified the Dominican Republic-Central America-United States Free Trade Agreement ("*CAFTA-DR*") in 2006. Despite these efforts, El Salvador's economic performance has been mixed. From 2000 to 2010, the Salvadoran economy averaged just 2 percent annual economic growth. In addition, foreign direct investment in El Salvador has lagged behind that of its Central American neighbors. Poverty rates have remained stubbornly high, reaching 35 per cent in 2012. The Government is determined to reverse these trends by laying the groundwork for a new cycle of investment and economic growth.

A Constraints Analysis ("*CA*") conducted in connection with the PfG identified two binding constraints to economic growth in El Salvador: (i) crime and insecurity; and (ii) low productivity in the tradables sector. In this context, the term "tradables" refers to goods and services that are traded internationally. The CA also found that human capital deficiencies, bureaucratic red tape, and high transportation and logistics costs are key factors that contribute to low productivity.

In November 2011, the USG and the Government adopted a Joint Country Action Plan ("*JCAP*") establishing goals and activities to unlock the constraints identified in the CA. The parties agreed to address crime and insecurity through programs to strengthen rule of law institutions and to prevent crime and violence. To improve productivity in the international trade of goods and services, the USG and the Government agreed to promote a business-friendly institutional environment, invest in human capital, and improve infrastructure. To foster a climate of trust, communication and collaboration between the Government and the business community, the Government established a growth council consisting of public officials and representatives of the private sector tasked with discussing challenges and developing options to

improve productivity (the “**Growth Council**”). Consistent with the JCAP, the program developed for the second Compact seeks to improve productivity by improving the investment climate, strengthening human capital, and reducing transportation and logistics costs. Through intensive policy reforms and an integrated set of investments in the human capital, physical capital, and institutional capital of El Salvador, MCC and the Government expect that the Compact will help set the foundation for lasting economic growth and poverty reduction in El Salvador.

(b) Consultative Process.

In 2012, the Government conducted an intensive consultative process prior to its submission of concept papers. The Government’s compact development team held meetings with a wide variety of groups that included business leaders, academia, women’s associations, industry groups and cooperatives engaged in international trade, and national and local government leaders. In addition, the team consulted with members of the Salvadoran diaspora living in the United States in order to gain input on reforms and changes that would spur greater interest in investing in El Salvador. The Government will ensure that consultations with civil society and local communities continue prior to and during implementation, with particular attention to the environmental and social impacts of investments in the coastal zone.

2. Description of Program and Beneficiaries.

(a) Description.

In furtherance of the Program Objective, the Parties have designed the Program to generate economic growth and poverty reduction in El Salvador by addressing the institutional, human and logistical constraints to El Salvador’s international trade in goods and services. The Program consists of three interrelated projects in furtherance of the Program Objective: (i) the Investment Climate Project; (ii) the Human Capital Project; and (iii) the Logistical Infrastructure Project.

Each Project is generally described in Part B of this Annex I. Part B also identifies one or more of the Activities that will be undertaken in furtherance of each Project as well as the various sub-activities within each Activity.

(b) Beneficiaries.

By improving the quality of education, reforming the business environment, and reducing transportation and logistics costs, the Program is expected to increase the productivity of firms engaged in the international trade of goods and services, which will increase current production, and subsequently, employment. The beneficiaries of this Compact are Salvadorans at the national level. The Compact is expected to contribute to overarching national-level benefits by promoting improvements in education policy and delivery, and greater transparency and efficiency in the public sector. These benefits include improved educational and curricular policies for human capital, signaling and demonstration effects that inform firms’ investment decisions in El Salvador, and institutional learning about how to develop and maintain public-private relationships. Specific beneficiaries are identified in greater detail in the Project descriptions in Part B of this Annex I.

3. Environmental and Social Performance; Gender Integration.

Unless MCC and the Government agree otherwise in writing, the Government will ensure that all Projects and Activities undertaken, funded or otherwise supported in whole or in part (directly or indirectly) by MCC Funding under this Compact comply with the MCC Environmental Guidelines, including the environmental and social performance standards set forth in the *Performance Standards on Environmental and Social Sustainability* of the International Finance Corporation (the “**IFC Performance Standards**”) that have been incorporated by reference into the MCC Environmental Guidelines. To that end, the Government will develop an environmental and social management system (“**ESMS**”) to ensure that the Projects and Activities comply with the MCC Environmental Guidelines including the IFC Performance Standards, as well as with all national environmental laws and regulations, licenses and permits, except to the extent such compliance would be inconsistent with this Compact. Specifically, the Government will: (a) cooperate with or complete, as the case may be, a strategic resettlement action plan (“**Strategic RAP**”), together with any ongoing environmental and social impact assessments, and if necessary, undertake and complete any additional environmental and social assessments and analyses, such as environmental and social management plans, environmental and social audits, and resettlement action plans (“**RAPs**”) required under the laws of El Salvador, the MCC Environmental Guidelines, this Compact, the PIA, or any other Supplemental Agreement, or as otherwise required by MCC, each in form and substance satisfactory to MCC; (b) ensure that Project or Activity-specific environmental and social management plans are developed and all relevant measures contained in such plans are integrated into project design, the applicable procurement documents and associated finalized contracts, in each case, in form and substance satisfactory to MCC; and (c) implement to MCC’s satisfaction appropriate environmental and social mitigation measures identified in such assessments or plans or developed to address environmental and social issues identified during compact implementation. Unless MCC agrees otherwise in writing, the Government will fund all necessary costs of environmental and social mitigation measures (including, without limitation, costs of resettlement) not specifically provided for, or that exceed the MCC Funding specifically allocated for such costs in, the Detailed Financial Plan (as defined in the PIA) for any Project or Activity.

To ensure social inclusion and gender integration across Projects and Activities, address human trafficking, and ensure compliance with the MCC Gender Policy and Gender Integration Guidelines, the Government will: (a) develop a comprehensive Social and Gender Integration Plan (“**Social and Gender Integration Plan**”) that, at a minimum: (i) identifies approaches for regular, meaningful and inclusive consultations with women and other vulnerable and/or underrepresented groups; (ii) sets forth strategies for consolidating the findings and recommendations of Project-specific social and gender analyses into final Project designs; and (iii) specifies actions to be taken during the course of the Compact; and (b) ensure, through monitoring and coordination during implementation, that final Activity designs, construction tender documents and implementation plans are consistent with and incorporate the outcomes of the social and gender analyses.

B. DESCRIPTION OF PROJECTS

Set forth below is a description of each of the Projects that the Government will implement, or cause to be implemented, using MCC Funding and the Government Contribution to advance the

applicable Project Objective. In addition, specific activities that will be undertaken within each Project (each, an “*Activity*”), including sub-activities, are also described.

1. Investment Climate Project.

(a) Summary of Project and Activities.

The Investment Climate Project is designed to increase private investment by improving El Salvador’s regulatory environment and institutional capacity and providing key public services in partnership with the private sector.

(i) Regulatory Improvement Activity.

The Regulatory Improvement Activity will prioritize and promote investment climate reforms resulting in more efficient and profitable business operations for firms doing business in El Salvador. Specifically, MCC Funding will support:

- the development of an institutional framework and system, including an institution to focus on regulatory improvement, and the prioritization and implementation of a select set of key reforms (the “*Institution*”); and
- a public-private dialogue to provide a transparent and user-driven input to the design and implementation of improved regulation, as well as public and private ownership and accountability for the reforms.

The reforms will focus on regulations and processes critical to El Salvador’s competitiveness in international markets, and may include trade facilitation, border crossing and customs procedures, environmental permitting and support for improved transparency and harmonization of municipal and national regulations. The Institution will also consider the extent to which regulations can be improved to reduce the potential for corruption. In designing and implementing reforms, the Institution will ensure that the proposed reforms are consistent with the Government’s obligations under international trade and investment agreements, including CAFTA-DR.

An interim, independent regulatory improvement entity will first be created under the Office of the President of El Salvador by executive decree. Thereafter, the permanent Institution will be created by law, will have technical autonomy and budget to execute its mandate, and will include sufficient private sector representation in its governance structure and be empowered by the Government for the regulatory review and prioritization process. The legal documentation creating the Institution and governing its operation will be in form and substance satisfactory to MCC.

In order to radically change perceptions of the investment climate in El Salvador and quickly and systematically improve the ease and cost of doing business, the Institution will undertake a comprehensive review of existing business laws and regulations and recommend the elimination or simplification of such laws and regulations in accordance with a transparent set of criteria established by the Institution. Any law or regulation that the Institution determines is unnecessary or obsolete will be recommended for elimination, and any law or regulation that is necessary but imposes unreasonable limitations on businesses will be recommended for simplification to the extent possible. The Government commits to adopt the initial

recommendations of the Institution and, within one year after the Compact enters into force, introduce a comprehensive package of reforms, including executive action and proposed legislation as necessary to implement such recommendations. The Institution will be empowered to make ongoing recommendations for regulatory improvement. Extensive stakeholder outreach and participation is critical to this process.

(ii) Partnership Development Activity.

The Partnership Development Activity is designed to enable the Government to partner with the private sector in innovative ways to provide key public goods and services needed to support private investment in the internationally traded goods and services sector.

Public-Private Partnerships Sub-Activity. The Public-Private Partnerships Sub-Activity seeks to enable the Government to use public-private partnerships (“*PPPs*”) to provide public goods and services. Specifically, MCC Funding will support:

- a general PPP capacity building program that develops the policies, procedures and training that Government agencies generally need to properly develop, implement and monitor PPPs, including support for the implementation of the *Ley Especial de Asocios Público Privados* (“*PPP Law*”), and any amendments thereto; and
- the development and tendering of two PPPs: the expansion of the El Salvador international airport (“*SAL*”), and the development of a wind farm in the Metapán region. This support will include the financing of studies to determine value for money of PPPs against traditional public financing, and engaging one or more transaction advisor(s), as necessary, to structure the optimal PPP model and bring it to market. In the event that the Parties determine that one or both of these projects is not viable, the Parties will identify another mutually acceptable project as a PPP that can be similarly developed and tendered within the Compact Term. Additional PPPs may be considered for inclusion in the Public-Private Partnerships Sub-Activity, subject to the availability of funds and written agreement between the Parties.

El Salvador Investment Challenge Sub-Activity. The El Salvador Investment Challenge Sub-Activity seeks to help the Government identify important private investment potential and efficiently allocate limited Government resources to public goods and services needed to support this investment. Specifically, MCC Funding and the Government Contribution will support:

- the development and financing of a joint MCC-Government investment facility – the El Salvador Investment Challenge (“*ESIC*”). ESIC will provide a transparent, open, fair, and competitive process to identify private investments in internationally-traded goods and services and will fund the necessary public and quasi-public components of selected projects to catalyze such private investments. The administration of ESIC will be governed by an operations manual, in form and substance satisfactory to MCC, setting forth, among others, eligibility criteria, requirements for economic rates of return, strong and effective governance and implementation structures, and transparency as to the selection of projects and use of ESIC funding (“*ESIC Operations Manual*”).

(b) Beneficiaries.

The beneficiaries of the Regulatory Improvement Activity are expected to be the firms operating in El Salvador (currently more than 25,000) who will experience fixed or variable cost savings as a result of the reforms. There are no anticipated direct beneficiaries of the PPP capacity building component of the Partnership Development Activity. The SAL expansion is expected to decrease delays and travel costs for travelers. The wind farm has no direct beneficiaries beyond workers who may see net income gains from employment at the project, but the project is expected to increase the Government's ability to attract investment for renewable energy. Beneficiaries of ESIC are expected to be those firms whose proposals are selected for grant funding, workers who realize net income gains associated with employment as a result of the projects, and third parties who benefit from the public investment.

(c) Environmental and Social Mitigation Measures; Gender Integration.

The Regulatory Improvement Activity is classified as Category "C" under the MCC Environmental Guidelines as the Activity is unlikely to have adverse environmental and social impacts.

Under the Partnership Development Activity, the PPP capacity building component is classified as Category "B" under the MCC Environmental Guidelines based on a preliminary assessment of environmental and social impacts. MCC Funding will only support the technical and financial planning to launch the SAL and wind farm PPPs, and not the PPPs themselves. The Government will incorporate MCC Environmental Guidelines including the IFC Performance Standards into relevant terms of reference for PPP due diligence studies for projects that benefit from MCC Funding. The findings and recommendations from applicable environmental and social impact assessment ("*ESIA*") and resettlement action plans will be incorporated into the structure of the PPP model, assigning responsibilities and allocating costs accordingly to public and private partners.

Under the Partnership Development Activity, the ESIC component is classified as Category "D" under the MCC Environmental Guidelines as the component will involve the creation of an intermediate facility to finance sub-projects that may potentially result in adverse environmental and social impacts. Under a Category "D" designation, ESIC financed projects must comply with minimum standards of impact analysis, IFC Performance Standards, on-going monitoring, and relevant laws and regulations of El Salvador.

The Regulatory Improvement Activity will take into consideration and address legal and regulatory barriers for businesses owned or operated by women and members of vulnerable groups in El Salvador. ESIC design and implementation will incorporate social and gender considerations, including that women and vulnerable groups have equal access and opportunity during the solicitation, application and selection phases of the ESIC.

(d) Donor Coordination.

In identifying and developing the Activities contemplated under the Investment Climate Project, the Government and MCC have coordinated with other donors that have particular expertise in, and/or are planning or funding, programs with a similar goal and nature. There are many donors and organizations involved in business environment improvement, yet there is not a process to prioritize efforts and review such projects. This Project will continue to require a high level of

donor and public sector coordination to ensure that all interested parties are supporting efforts to increase investment, employment, and economic growth.

The Regulatory Improvement Activity also builds on the work and is structured to collaborate with the Growth Council established under the JCAP. Separately, the Institution, which is responsible for continuous regulatory improvement, will allow for dialogue and concrete action to reform laws and regulations, and increase the efficiency and competitiveness of El Salvador.

The Partnership Development Activity builds on the work of the JCAP, which encourages the use of PPPs to expand SAL and the development of renewable energy projects to reduce production costs and increase investment in the international trade of goods and services.

(e) USAID.

MCC and the Government have coordinated with the United States Agency for International Development (“*USAID*”) through the PfG process and the JCAP. In particular, MCC and USAID have coordinated and will continue to coordinate with respect to USAID’s Municipal Competitiveness Project, Small and Medium Enterprise Development Project, and Regional Trade and Market Alliances Project. MCC also coordinated Project development with USAID and United States Environmental Protection Agency (EPA) on strengthening the *Sistema Nacional de Gestión Ambiental* (SINAMA) in order to improve Government capacity for environmental permitting.

(f) Sustainability.

The Investment Climate Project is premised on the idea that private investment is the primary engine of sustainable economic growth. The Investment Climate Project is focused on strengthening regulatory efficiency and institutional capacity in core areas that most impact private sector operation and expansion – key ingredients to promoting investment and real growth. The Investment Climate Project also facilitates specific transactions that attract private investment, improve the infrastructure base on which private sector-led growth depends, and improve the perception of the country as investment-friendly.

(g) Policy, Legal and Regulatory Reforms.

The Parties have identified the following policy, legal and regulatory reforms and actions that the Government will pursue in support, and to reach the full benefits, of the Investment Climate Project:

- The Government will ensure the availability of funding to support regulatory improvements identified as priority reforms by the Institution whose costs exceed the amount of MCC Funding allocated hereunder;
- The Government will adopt the initial recommendations of the Institution and, within one year after the Compact enters into force, introduce a comprehensive package of reforms, including executive action and proposed legislation as necessary to implement such recommendations.
- The Government will (i) support legislation in furtherance of any joint proposal by the Government and the Growth Council to strengthen the PPP Law to increase El Salvador’s

competitiveness, and (ii) adopt regulations in furtherance of the PPP Law which are mutually acceptable to the Parties;

- The Government, through MCA-El Salvador, will convene a donor working group specific to regulatory improvement to ensure alignment with the Investment Climate Project; and
- The creation and operation of the Institution pursuant to this Compact, adoption of reforms and the Government's approval of the ESIC Operations Manual will be conditions to specified Disbursements for this Project, as further defined in the Program Implementation Agreement.

2. Human Capital Project.

(a) Summary of Project and Activities.

The Human Capital Project is designed to improve the quality of education and to better match the supply of skills relevant to the international trade of goods and services in El Salvador to the demand of the labor market. The Human Capital Project consists of two Activities: the Education Quality Activity and the Technical Vocational Education and Training (“*TVET*”) System Reform Activity. To ensure the success and sustainability of this Project, the Government commits to provide funding complementary to, and in support of, MCC's investments under this Project. The Government's funding commitment includes continued post-Compact support for reforms designed or implemented under each Activity and the maintenance of infrastructure and equipment funded under the Compact, as further articulated below.

(i) Education Quality Activity.

Under this Activity, MCC Funding and the Government Contribution will support complementary interventions to provide Salvadoran students the benefits of competency-based education, increased classroom time, teachers trained in requisite subject-matters and pedagogical skills, and an institutional and physical environment that is conducive to learning.

Strengthening the National Education System Sub-Activity. This Sub-Activity seeks to improve the effectiveness and quality of the national education system in El Salvador. Specifically, MCC Funding will support legal, policy and operational reforms for the educational system through the Government's Ministry of Education (“*MINED*”), including the following:

- teacher continuous professional development, assessment, and performance monitoring;
- the measurement and use of national student learning and achievement data;
- information systems governance and data quality assurance;
- curricula development and the establishment of a National Curriculum Evaluation Commission;
- the establishment of school management committees; and

- the development of a MINED gender policy in form and substance satisfactory to MCC, and phased implementation in accordance with its terms and conditions.

Implementation of Full-Time Inclusive Model Sub-Activity. This Sub-Activity seeks to strengthen and expand the implementation of a full-time inclusive school model. MCC Funding will support the implementation of the full-time inclusive school model in an estimated 55 clusters (schools grouped together according to spatial proximity and other organizational aspects), focusing resources at the third cycle and high school levels (grades 7-12). The methodology to organize and select clusters, and implementation of the MCC funded intervention will be subject to agreement between the Parties. Specifically, MCC Funding will support:

- establishment of a general and/or technical high school in each cluster;
- the construction and/or rehabilitation of infrastructure to provide facilities appropriate for the selected clusters;
- professional development of all teachers and school administrators in selected clusters;
- curricula learning plans that foster active learning methods and ongoing classroom-based student assessment;
- strengthening of learning in the classroom in subject matter areas of English, mathematics, science and information technology, and such 21st century learning, innovation, life and career skills;
- the establishment and training of school management committees;
- an increase in the school day from 25 to 40 hours per week; and
- the provision of educational materials and equipment.

(ii) TVET System Reform Activity.

The TVET System Reform Activity seeks to harmonize the skills supplied by private and public education and training providers with the skills demanded by the labor market. The detailed design and implementation of the TVET System Reform Activity will be informed by the results of the ongoing studies funded as part of the development of this Compact.

Integrated TVET Governance System Sub-Activity. This Sub-Activity seeks to strengthen the national TVET governance system by supporting legal, policy and operational reforms within the system. Specifically, MCC Funding will support:

- with the coordination of the Technical and Planning Secretariat of the President and with the advice of the Growth Council, the establishment of and funding for an entity acceptable to the Parties and governed by a board comprised of an equal number of public and private sector representatives to provide the legal and institutional framework for an integrated TVET system (“**TVET Governing Body**”);

- TVET competency-based curricula development, with participation and assumed responsibilities from the private sector;
- career orientation services, including career counseling and job matching services;
- promoting a blend of school- and industry-based training and workforce development initiatives; and
- the establishment of a framework and standards for accreditation of TVET training organizations, and certification of teachers and students.

TVET Continuous Labor Demand Assessment Sub-Activity. This Sub-Activity seeks to strengthen the capacity of the TVET system for identifying labor market trends that will inform the strategic direction of the TVET system. Specifically, MCC Funding will support:

- the establishment of an M&E framework, and
- the establishment of a labor market observatory, integrating existing similar efforts.

(b) Beneficiaries.

Direct beneficiaries of the Project are expected to be students in seventh through twelfth grades, in general and technical education, who realize higher incomes as a result of their greater years of education. In particular, the Project is expected to contribute to preventing or postponing the dropout of as many as 176,000 seventh to twelfth graders. Direct beneficiaries of the TVET System Reform Activity are expected to be TVET students who receive higher incomes as a result of receiving skills that are better matched to labor market needs.

Additional beneficiaries of the Project may include students who do not attend a full-time inclusive school, but receive increased incomes as a result of improved quality of education that result from the national reforms implemented by MINED under this Compact. Communities may experience reductions in crime as a result of the full-time inclusive school model, due to increased permanence of students in school which is expected to reduce their social vulnerability.

(c) Environmental and Social Mitigation Measures; Gender Integration.

The Human Capital Project overall is classified as a Category “B” project under the MCC Environmental Guidelines. However, the non-infrastructure activities within this Project are Category “C” activities given that they are unlikely to have adverse environmental impacts.

The key environmental risks associated with the Human Capital Project include the provision of environmental, occupational health and safety, and hazardous and non-hazardous waste management during school infrastructure rehabilitation activities, and the safety of workers, equipment and beneficiaries given the high levels of crime and violence in El Salvador. As part of the Strategic RAP, the Government, through MCA-El Salvador, MINED and El Salvador’s national land registry center (*Centro Nacional de Registro* or *CNR*), will resolve potential land titling issues of schools that benefit from MCC funded infrastructure construction or rehabilitation. No works for any school under this Project may commence without resolution of the title for that school. Otherwise, the land titling of properties will need to be clarified and resolved for all schools affected by the Project, including that MINED confirms that it will

finance operations and maintenance (“*O&M*”) in schools that benefit from MCC Funding, the terms of which will be subject to a condition precedent, that will be defined in the PIA.

MCA-El Salvador will develop an Environmental and Social Assessment (“*ESA*”) and an Environmental and Social Management Framework (“*ESMF*”) to address the overall environmental and social issues associated with the school rehabilitation program, identify, screen and assess key risks, and propose appropriate measures to manage such risks and impacts. The ESA and ESMF will focus on qualitative impacts and general rules, regulations, and management and mitigation measures rather than on quantifying the impacts of site-specific interventions.

MCC Funding will support specific gender and social integration strategies for each component of the Education Quality Activity, including teacher professional development, curricula development, and implementation of the full-time inclusive school models. In addition, MCC Funding will support the development of a gender policy for MINED and an implementation plan or strategy for that policy under the Education Quality Activity. The TVET System Reform Activity will take into consideration social and gender factors in the development of El Salvador’s TVET governance system, as well as gender integration in the TVET labor demand assessment, curricula and learning method development and training, and standards for student and teacher certification.

(d) Donor Coordination.

MCC and the Government have coordinated the development of the Human Capital Project with other donors in El Salvador, including the World Bank and USAID. The Government plans to adopt the full-time inclusive school model nationally and is working with multiple donors in addition to MCC, including USAID, the Italian Development Cooperation and the World Bank, to expand implementation of the model across El Salvador.

(e) USAID.

Through the PfG and the JCAP, MCC and USAID have worked closely to ensure coordination of efforts in the education sector, and share lessons learned. The MCC-supported Human Capital Project will focus on skill constraints to improving productivity and innovation in the international trade in goods and services – which are English, math, science, IT and other 21st century learning, innovation, life and career skills. MCC investments will be directed at grades 7-12, a critical time when students must develop the employability skills necessary for a successful transition into the workplace. In this regard, the Project builds on earlier USAID investments in basic education at the primary school level (grades 1-6) focused on strengthening language and literacy skills. The MCC investments will also complement USAID’s TVET investments at the post-secondary level.

The Human Capital Project will support policy reforms to improve governance of both the education system in general and the TVET system in particular, which will benefit both USAID and MCC funded programs. Both agencies are supporting MINED’s strategy of transitioning to a full-time school model that will have benefits for both the international trade in goods and services and security constraints of PfG. MCC and USAID will seek to harmonize existing reporting frameworks for this model, and combine resources to strengthen M&E capabilities at MINED.

(f) Sustainability.

The Project focuses on national policy reform and institutional strengthening, both of which are critical to long-term sustainability. El Salvador's national education strategy supports both Activities. To further demonstrate the Government's long-term commitment to the sustainability of the Project, the Government commits to provide the funding necessary to support the long-term viability and utility of the interventions contemplated herein.

The sustainability of the Human Capital Project relies on the MCC-funded establishment of the National Curriculum Evaluation Commission and the TVET Governing Body under both Activities. These entities will ensure continuing quality assurance and administration of improved quality of general education and demand-driven TVET. In a further effort towards sustainability, a tapering assistance model will be applied for the staffing of these entities and the Government will assume an increasing percentage of related costs and salaries under the Compact, so that by the fourth year of the Compact Term, the Government will have assumed all such costs. The sustainability of MCC-funded clusters will benefit from student, community and school personnel input through school management committees. The Government will fund stipends for school lunches and transportation for vulnerable students in full-time inclusive schools.

The Government and MCC recognize that the intended outcomes of the Project – such as higher educational attainment, longer school days, expanded teacher training, and participation in international testing – will lead to increased fiscal responsibilities for MINED. During the Compact Term, implementation of the Activities will be structured such that MCC Funding will be used for discretionary, non-recurring investments, including the establishment of the National Curriculum Evaluation Commission and TVET Governing Body, creation of teacher and student certification systems, development of learning plans, and school rehabilitation, while Government-MINED funds will be used to support recurring costs. MINED will provide funding for all teacher and school administrator salaries, including the additional personnel required in the clusters, and will also cover all O&M costs associated with implementation of the full-time inclusive school model and at least half of the costs to train teachers and school administrators through its Government Contribution. MCC will continue to work with MINED on incremental cost requirements and sustainability plans. MINED's policy and procedures for school O&M and its mechanism for providing budget to each school will be reviewed and revised in accordance with paragraph 2(g) of Part B of this Annex I.

MCC will work with the Government to evaluate its expenditures on education. In general, El Salvador invests less in education than other countries in the region as a percentage of GDP. To ensure the sustainability of the investments under this Compact, the Government needs to increase the resources available to the education sector within a process of improving educational outcomes, to complement implementation of the Human Capital Project. MCC will work with the Government under the Compact on increasing public resources dedicated to education.

(g) Policy, Legal and Regulatory Reforms.

As noted above, the Government's national education strategy demonstrates a commitment to policy and institutional changes that justify the Compact's investment in the Human Capital

Project. The Parties have identified and agreed on the following policy, legal and regulatory reforms and actions necessary for the success of the Project:

- The Government agrees to a randomized control trial of the full-time inclusive school model, including restrictions on implementing the model in the control groups established by an independent evaluator, unless deemed impractical by both Parties.
- MCC and the Government will review the adequacy and efficacy of the Government's public education expenditures on an annual basis. In so doing, during the Compact Term, MINED, through MCA-El Salvador, will submit for MCC review and approval the budget estimates for incremental recurring costs (i.e. salaries and O&M) associated with the implementation of Full-Time Inclusive Model Sub-Activity. In addition, the Government will provide the necessary resources, as agreed with MCC, to sustain each Activity's legal, policy and operational reforms, and to permit the continued work of the National Curriculum Evaluation Commission and the TVET Governing Body.
- MCC will work with the Government to ensure that primary education expenditures are reported to UNESCO in a manner that allows MCC to include such data in its annual scorecard of candidate countries.
- MCC will work with MINED to identify a plan to establish periodicity of national tests (e.g., PAESITA, El Salvador's national aptitude test for primary and middle school students) and participation and funding in international tests (e.g., TIMSS, OREALC/UNESCO, PISA), as agreed between the Parties.
- The Government and MCC will review the current professional development plan, and make revisions and modifications, if necessary (including incentives for long-term professional development), to ensure the functioning of a high-quality education system. Agreement between the Parties as to the plan will be a condition precedent, to be defined in the PIA.
- The Government will ensure that MINED strengthens its O&M planning and administration for education infrastructure of the full-time inclusive school clusters to ensure adequate support of those clusters ("**O&M Plan**"). The Government will provide a budget allocation for such clusters consistent with the O&M Plan. The Government's obligations to develop the O&M Plan and apportion the budget allocation will be a condition precedent for Disbursement under this Project, to be defined in the PIA.
- With respect to school infrastructure constructed or rehabilitated under this Project, the Government will provide resources sufficient to maintain such infrastructure for its intended useful life in accordance with the O&M Plan. The Government's resource-allocation obligation will be a condition precedent for Disbursement under this Project, to be defined in the PIA.

3. **Logistical Infrastructure Project.**

(a) Summary of Project and Activities.

The Logistical Infrastructure Project comprises two Activities designed to reduce logistical and transportation costs and to increase investment and productivity in the trade of goods and services. The Project seeks to relieve bottlenecks at critical sections of the logistical corridors between the main border crossing with Honduras at El Amatillo, the Ports of La Union and Acajutla, and the international airport.

(i) Coastal Highway Expansion Activity.

The Coastal Highway Expansion Activity seeks to relieve congestion at the most-trafficked segment of El Salvador's coastal highway ("CA-2"). The CA-2 is one of the two most important logistical corridors in the country and connects the country's major logistical nodes, including its two sea ports (La Union and Acajutla) and SAL. The Activity will finance three segments of CA-2: the 7.22 kilometer segment from Comalapa to La Herradura, the 16.98 kilometer segment from La Herradura to Zacatecoluca, and the 2.97 kilometer segment from La Libertad intersection to the Comapala Airport Road intersection. Specifically, MCC Funding and the Government Contribution will support:

- implementation of construction activities for the opening, improvement, or rehabilitation of the segments stipulated above;
- implementation of environmental and social mitigation measures as identified in the ESIA's, Strategic RAP, and specific RAPs, or as otherwise may be appropriate;
- Project management, supervision, technical services required for implementation, and auditing, as appropriate; and
- technical assistance to improve operations of the national road maintenance fund, the *Fondo de Conservación Vial* ("**FOVIAL**").

The Government is financing the feasibility study, detailed design and ESIA for the three segments of the Coastal Highway Expansion Activity. If, as a result of such studies or after receipt of bids for any segment, MCC determines in consultation with MCA-El Salvador, that the costs of the Activity will likely be in excess of the budget for this Activity, including the Government Contribution, MCC and the Government will modify the Activity through a reduction of scope and/or value-engineering in a manner that seeks to fulfill the Activity objective while maintaining an anticipated ERR of at least 10 percent.

(ii) Border Crossing Infrastructure Activity.

The Border Crossing Infrastructure Activity seeks to relieve the freight and passenger traffic congestion at the border crossing into Honduras at El Amatillo by: (A) rehabilitating and improving up to a 5.74 kilometer road from Agua Salada to El Amatillo; and (B) improving and modernizing the border crossing facilities on the Salvadoran side of the La Amistad Bridge and the site on the Pan American Highway. Specifically, MCC Funding and the Government Contribution will support:

- implementation of construction activities for the improvement, and rehabilitation of the road from Agua Salada to El Amatillo;
- land acquisition (including RAP implementation, as applicable) for the road and one control center (with two control stations);
- implementation of environmental and social mitigation measures as identified in the ESIA's, Strategic RAP, and specific RAPs, or as otherwise may be appropriate;
- the construction of the control center, including buildings, internal access and connecting roads, parking areas, stormwater drainage, potable water supply system, wastewater treatment plant, lighting, and other infrastructure components that may be necessary for the effective functioning of these control stations; and
- Project management, supervision, technical services required for implementation, and auditing, as appropriate.

To ensure compliance with Section 2.7 of this Compact, the Government Contribution will finance the costs of construction for those portions of the control stations destined exclusively for use by the national police. The calculation of such costs will be determined consistent with a formula based on the final designs and agreement of the Parties.

(b) Beneficiaries.

The beneficiaries for the proposed Logistical Infrastructure Project are the estimated 171,159 individuals living within five kilometers of either side of the Project construction. Because of the nature of the proposed Activities as key logistical thoroughfares, benefits in the form of reduced vehicle operating costs and travel time are expected to accrue to individuals and firms that travel along those corridors each day.

(c) Environmental and Social Mitigation Measures; Gender Integration.

The Coastal Highway Expansion Activity is classified as a Category “A” project under the MCC Environmental Guidelines as it involves the widening of an existing road to provide four lanes, along more than 10 continuous kilometers of roadway. The principal environmental and social concerns include traffic safety, hydrology and resettlement. The road expansion will take place on land that is included in approved municipal land use plans and covered by the Strategic Environmental Assessment (“*SEA*”) of the Marine-Coastal Zone Development Plan. During detailed design, route alternatives will be evaluated with participation of municipal planning bodies. The detailed design will also consider, as appropriate, potential cumulative impacts of the economic development expected to be generated as a result of the highway expansion and to determine any enhancement, mitigation or compensatory measures that may be needed in compliance with the recommendations of the SEA.

The Border Crossing Infrastructure Activity is categorized as a Category “B” project under the MCC Environmental Guidelines as the length of the road to be financed is less than 10 continuous kilometers. Issues that would be addressed in detailed design of this Activity are similar to those in the Coastal Highway Expansion Activity, including traffic safety, hydrology and resettlement. In response to the incidence of HIV/AIDS at the El Amatillo border crossing, prevention and management plans for HIV/AIDS will be developed and implemented for local

populations, as well as construction workers who will come into the area for the Border Crossing Infrastructure Activity.

For both activities, ESIA's will be contracted by the Ministry of Public Works (“**MOP**”) as part of the feasibility and design studies. The Government will ensure that all studies comply with MCC Environmental Guidelines (including the IFC Performance Standards). Specific environmental management plans must be prepared for each activity to ensure enhancement of positive impacts and to specify avoidance, mitigation, and management measures for negative impacts. Consultation and stakeholder engagement plans, as well as grievance mechanisms for local populations and workers, are also expected outputs of the ESIA.

The Social and Gender Integration Plan will also include prevention and management plans for social and gender risks related to trafficking in persons (“**TIP**”), which includes prostitution, at the El Amatillo border crossing under the Border Crossing Infrastructure Activity. The long wait times currently experienced by truckers at the El Amatillo border crossing exacerbates trafficking and prostitution problems at the border crossing. MCA-El Salvador will also explore mechanisms for creating employment opportunities for women during Project implementation.

(d) Donor Coordination.

MCC has actively engaged multilateral and bilateral donors financing road infrastructure in El Salvador to discuss possible policy and operational reforms to attain sustainable road maintenance. Such donors include the Central American Bank for Economic Integration, the World Bank, the Inter-American Development Bank (“**IDB**”), the United Nations Development Programme, and the Japan International Cooperation Agency. MCC, in coordination with these donors, will work with the Government to help develop policy and operational reforms to address the long-term sustainability of the Project’s proposed investments and the road network of El Salvador. Additionally, MCC and IDB plan to establish routine in-country coordination about other investment areas of common interest such as PPPs.

(e) USAID.

USAID does not focus on transport infrastructure and logistics in El Salvador. USAID, through the Regional Trade and Market Alliances Project, will support capacity building activities on trade facilitation to Customs and other border control agencies, in Central American borders, including El Amatillo. MCC, USAID and the Government will work through the JCAP, as appropriate, to identify potential opportunities for coordination in these sectors.

(f) Sustainability.

MOP is the Government entity responsible for planning, rehabilitating, improving, and expanding the national road network. MOP plays an important role in the coordination and oversight of the activities of FOVIAL. The roads financed under the Logistical Infrastructure Project will be under FOVIAL’s maintenance jurisdiction, and therefore the Government will allocate sufficient budget, including any increase in the budget as may be necessary, for FOVIAL to maintain the national road network in accordance with international best practices, as further stipulated in paragraph (3)(g) of Part B of this Annex I below.

(g) Policy, Legal and Regulatory Reforms.

The Parties have identified and agreed on the following policy, legal and regulatory reforms and actions necessary for the success of the Project: As soon as practicable after this Compact becomes provisionally applicable in accordance with Section 7.5, the Government will commission an independent study acceptable to MCC that will determine, among other matters, the legal, institutional and financial reforms required to ensure the sustainability of the road network for which FOVIAL is legally responsible, in accordance with international best practices, including the appropriate level of road maintenance funding for FOVIAL (the “**Road Maintenance Study**”).

Prior to the release of bidding documents for works on the Coastal Highway Expansion Activity, the Government will provide evidence acceptable to MCC that the Government has adopted the recommendations of the Road Maintenance Study, including the passage by the *Asamblea Legislativa* of necessary legal reforms; *provided that*, if such reforms are not adopted, the Government will have increased its annual budget allocation to FOVIAL exclusively for road maintenance by (i) at least 20 percent over the amount allocated for such purpose during the preceding fiscal year or (ii) the amount set forth in the Road Maintenance Study, whichever is less. For the avoidance of doubt, such budget will exclude any amounts for servicing outstanding loans or other indebtedness.

C. IMPLEMENTATION FRAMEWORK

1. MCA-El Salvador.

(a) Structure and Establishment.

The Government will establish an accountable entity, MCA-El Salvador, as an autonomous entity of public nature and utility under the laws of El Salvador. MCA-El Salvador will not be under the control of any state controlling body and it will have operational and legal independence, including, *inter alia*, the ability to (i) enter into contracts in its own name; (ii) sue and be sued; (iii) establish a bank account in its own name; (iv) expend MCC Funding and the Government Contribution; and (v) engage contractors, consultants and/or grantees, including, without limitation, a procurement and fiscal agent. The Government will include MCA-El Salvador with respect to the Government’s coordination of bilateral or multilateral development assistance projects related to the Program.

MCA-El Salvador’s internal operations will be governed by the law creating it, and by bylaws issued by Presidential decree, which will provide further detail on the internal operations of MCA-El Salvador, each in form and substance satisfactory to MCC.

MCA-El Salvador will be administered, managed, and supported by the following bodies: (i) a board of directors (the “**Board of Directors**”); (ii) a management team; and (iii) one or more Stakeholders Committees (as defined below).

(b) Board of Directors.

The Board of Directors will have ultimate responsibility for the oversight, direction, and decisions of MCA-El Salvador, as well as the overall implementation of the Compact. The Board of Directors will be comprised of seven voting members, plus three or more non-voting

members. The voting members of the Board of Directors will include the following representatives / offices:

- (i) Technical and Planning Secretary to the President, who will also serve as Chair of the Board;
- (ii) Minister of Education (MINED);
- (iii) Minister of Public Works (MOP);
- (iv) Representative of El Salvador Export and Investment Promotion Agency (PROESA);
- (v) Representative of an environmental or gender-focused non-governmental organization;
- (vi) Representative of academic institution or think tank; and
- (vii) Representative of the private sector, nominated by the Growth Council.

The members of the Board of Directors may be represented by alternates appointed pursuant to MCA-El Salvador's governing documents. In addition, an MCC representative, MCA-El Salvador's Executive Director, a representative of the Ministry of the Environment (MARN) and other NGO, government or municipality representatives may serve as non-voting members of the Board, as agreed by the Parties.

(c) Management Team.

The Management Team, as defined below, will report to the Board of Directors and will have principal responsibility for the day-to-day operations and management of the Compact, including contracting, program management, financial management, reporting, and monitoring and evaluation. As a recipient of MCC Funding, MCA-El Salvador will be subject to MCC audit requirements.

The Management Team will be led by an Executive Director and is composed of the following directors and officers: a Deputy Executive Director – Program Implementation, Deputy Executive Director – Operations & Evaluation, Legal Advisor, Communications Director, Internal Auditor, Human Capital Project Director, Infrastructure Director, Investment Climate Project Director, Gender and Social Impact Director, Environmental and Social Performance Director, Human Resources Director, Finance Director, Administration Director, Procurement Director, and Monitoring & Evaluation Director (the “*Management Team*”). The Management Team will be selected after an open and competitive recruitment and selection process (or its equivalent), and the appointment of each member of the Management Team is subject to MCC approval. The directors will be supported by appropriate additional staff to enable the Management Team to execute its roles and responsibilities. Upon written notice by MCC to MCA-El Salvador, the selection of candidates for additional positions within MCA-El Salvador will be subject to MCC approval.

(d) Stakeholders' Committee(s).

(i) Composition. MCA-El Salvador will be assisted by one or more stakeholders' committees, (each a "***Stakeholders' Committee***"), which will be created according to a process in accordance with MCC's Governance Guidelines, as approved by MCC. Without limiting the foregoing, as required in MCC's Governance Guidelines, each Stakeholders' Committee will be composed of *inter alia*, program beneficiaries, regional and local government representatives, entities with an interest or involvement in the implementation of the Compact, key NGOs, and any applicable civil society and private sector representatives.

(ii) Roles and Responsibilities. The Stakeholders' Committee(s) will be responsible for continuing the consultative process throughout implementation of the Compact. While the Stakeholders' Committee(s) will not have any decision-making authority, the Stakeholders' Committee(s) will be responsible for reviewing, at the request of the Board or the Management Team, certain reports, agreements, and documents related to the implementation of the Compact in order to provide advice and input to MCA-El Salvador regarding the implementation of the Program.

2. Implementing Entities.

Subject to the terms and conditions of this Compact, the Program Implementation Agreement and any other related agreement entered into in connection with this Compact, the Government may engage one or more entities of the Government to implement and carry out any Project or Activity (or a component thereof) under this Compact (each, an "***Implementing Entity***"). The appointment of any Implementing Entity will be subject to review and approval by MCC. The Government will ensure that the roles and responsibilities of each Implementing Entity and other appropriate terms are set forth in an agreement, in form and substance satisfactory to MCC (each an "***Implementing Entity Agreement***").

3. Fiscal Matters.

(a) Fiscal Agent. The Government will ensure that, pursuant to the bylaws or any other governing document as necessary, MCA-El Salvador appoints its financial management unit (*Dirección Financiera*) ("***DF***") as its fiscal agent (a "***Fiscal Agent***") and grants to DF all power and rights necessary to perform the function of the Fiscal Agent, as such are set forth herein, in the Fiscal Accountability Plan and in any Supplemental Agreement or Implementation Letter. The Fiscal Agent will be responsible for, among other things: (i) assisting MCA-El Salvador in preparing the Fiscal Accountability Plan; (ii) ensuring and certifying that Disbursements are properly authorized and documented in accordance with established control procedures set forth in the Program Implementation Agreement and other Supplemental Agreements; (iii) Disbursement from, and cash management and account reconciliation of, any Permitted Account established and maintained for the purpose of receiving Disbursements and making payments (to which the Fiscal Agent has sole signature authority); (iv) providing applicable certifications for MCC Disbursement Requests; (v) maintaining and retaining proper accounting, records and document disaster recovery system of all MCC-funded financial transactions and certain other accounting functions; (vi) producing reports on Disbursements (including any requests therefor) in accordance with established procedures set forth in the Program Implementation Agreement, the Fiscal Accountability Plan, or any other Supplemental Agreements; (vii) assisting in the preparation of budget development procedures; and (viii)

internal management of the Fiscal Agent operations. Upon the written request of MCC for DF to be replaced as the Fiscal Agent, the Government will ensure that MCA-El Salvador engages a new Fiscal Agent, subject to approval by the Board of Directors and MCC; *provided, however*, that the Government will ensure that DF continue to perform its obligations as the Fiscal Agent until MCA-El Salvador has engaged a successor Fiscal Agent. In the event that a party other than DF is the Fiscal Agent, upon the written request of MCC, the Government will ensure that MCA-El Salvador terminates the Fiscal Agent, without any liability to MCC, and the Government will ensure that MCA-El Salvador engages a new Fiscal Agent, subject to approval by the Board of Directors and MCC. The Government will ensure that MCA-El Salvador enters into an agreement with each Fiscal Agent other than DF, in form and substance satisfactory to MCC, that sets forth the roles and responsibilities of the Fiscal Agent and other appropriate terms and conditions, such as payment of the Fiscal Agent (each, a “***Fiscal Agent Agreement***”). Such Fiscal Agent Agreement will not be terminated until MCA-El Salvador has engaged a successor Fiscal Agent or as otherwise agreed by MCC in writing.

(b) **Fiscal Oversight Agent**. The Government will ensure that MCA-El Salvador engages an agent through an international competitive process (the “***Fiscal Oversight Agent***”) to carry out and certify certain financial management activities in furtherance of this Compact. The role and responsibilities of such Fiscal Oversight Agent and the criteria for selection of a Fiscal Oversight Agent will be as set forth in the applicable Implementation Letter or Supplemental Agreement. The Government will ensure that MCA-El Salvador enters into an agreement with the Fiscal Oversight Agent, in form and substance satisfactory to MCC, that sets forth (i) the roles and responsibilities of the Fiscal Oversight Agent with respect to the oversight of the Fiscal Agent and the monitoring and review of the Fiscal Agent’s compliance with the Fiscal Accountability Plan; and (ii) other appropriate terms and conditions, such as payment of the Fiscal Oversight Agent (the “***Fiscal Oversight Agreement***”).

4. Procurement Agent.

Based upon an assessment of local capacity and previous experience from the first compact, an internal MCA-El Salvador procurement unit will manage Compact procurements. A procurement director who has the requisite skills and experience to manage the procurement processes planned for this Compact (the “***Procurement Director***”) will be hired by MCA-El Salvador. The Procurement Director will also manage the procurement staff required to implement the procurements carried out under the compact. The Procurement Director will ensure that MCA-El Salvador adheres to the procurement standards set forth in the MCC Program Procurement Guidelines and ensure procurements are consistent with the procurement plan adopted by the Government pursuant to the Program Implementation Agreement, unless MCC agrees otherwise in writing. In its discretion, MCC may require that the Government engage an independent procurement agent during the Compact Term.

5. Dissolution of MCA-El Salvador.

MCA-El Salvador will cease to exist by operation of law upon the expiration of the Compact Term and any further period stipulated pursuant to Section 5.2(a) of this Compact. The Government and MCC will agree on the assignment to other Government entities of any rights, obligations and liabilities of MCA-El Salvador that may accrue as a result of the dissolution of MCA-El Salvador.

6. Access to Information.

MCA-El Salvador will be subject to this Compact, the Program Implementation Agreement, the Program Guidelines and any Implementation Letter in connection with the maintenance of records and rights of access to such records. To the extent that the obligations contained in such Compact-related documents conflict with the laws of El Salvador, the Compact-related obligations will prevail.

ANNEX II

MULTI-YEAR FINANCIAL PLAN SUMMARY

This Annex II summarizes the Multi-Year Financial Plan for the Program.

1. General.

A multi-year financial plan summary (“*Multi-Year Financial Plan Summary*”) is attached hereto as Exhibit A to this Annex II. By such time as specified in the Program Implementation Agreement, the Government will adopt, subject to MCC approval, a multi-year financial plan that includes, in addition to the multi-year summary of estimated MCC Funding and the Government’s contribution of funds and resources, the annual and quarterly funding requirements for the Program (including administrative costs) and for each Project, projected both on a commitment and cash requirement basis.

2. Government LMIC Contribution.

During the Compact Term, the Government will make contributions, relative to its national budget and taking into account prevailing economic conditions, as are necessary to carry out the Government’s responsibilities under Section 2.6(a) of this Compact. These contributions may include in-kind and financial contributions (including obligations of El Salvador on any debt incurred toward meeting these contribution obligations). In connection with this obligation the Government has developed a budget over the Compact Term to supplement MCC Funding through direct financial contributions toward expenditures of MCA-El Salvador or as otherwise agreed by the Parties in writing. The Government contributions are anticipated to support: teacher training, infrastructure maintenance, stipends for student transportation and meals, and other costs to finance the costs related to additional enrollment and the TVET Governance Body for the Human Capital Project; investment commitment for the Partnership Development Activity under the Investment Climate Project; the Coastal Highway Expansion Activity and the Border Crossing Infrastructure Activity under the Logistical Infrastructure Project; and expenses for Program administration and oversight. To this end, the Government anticipates making contributions of at least US\$88,200,000 over the Compact Term (the “*Government Contribution*”). This Government Contribution will be in addition to the Government’s spending allocated toward the Project Objectives in its budget for the year immediately preceding the establishment of this Compact. The Government Contribution will be subject to any legal requirements in El Salvador for the budgeting and appropriation of such contribution, including approval of the Government’s annual budget by its legislature. The Parties may set forth in the Program Implementation Agreement or other appropriate Supplemental Agreements certain requirements regarding the Government Contribution, which requirements may be conditions precedent to the Disbursement of MCC Funding. During implementation of the Program, the Government Contribution may be modified or new contributions added with MCC approval; *provided that*, the modified or new contributions continue to advance the Project Objectives.

EXHIBIT A TO ANNEX II
MULTI-YEAR FINANCIAL PLAN SUMMARY

| EL SALVADOR II - MULTI-YEAR FINANCIAL PLAN | | | | | | | | |
|---|-------------|-------------|-------------|-------------|-------------|-------------|--------------|-------------|
| (in million US\$) | | | | | | | | |
| Component | CIF | Year 1 | Year 2 | Year 3 | Year 4 | Year 5 | MCC Total | Government |
| 1. Investment Climate Project | | | | | | | | |
| Activity 1: Regulatory Improvement | 1.3 | 1.0 | 1.1 | 1.1 | 0.9 | 0.6 | 6.0 | |
| Activity 2: Partnership Development | 2.0 | 8.9 | 10.7 | 5.4 | 5.4 | 4.0 | 36.4 | |
| Sub-total | 3.3 | 9.9 | 11.8 | 6.5 | 6.3 | 4.6 | 42.4 | 50.0 |
| 2. Human Capital Project | | | | | | | | |
| Activity 1: Education Quality | 0.7 | 4.3 | 15.3 | 22.9 | 31.5 | 10.5 | 85.2 | |
| Activity 2: TVET System Reform | 0.2 | 1.8 | 3.8 | 3.8 | 3.8 | 2.1 | 15.5 | |
| Sub-total | 0.9 | 6.1 | 19.1 | 26.7 | 35.3 | 12.6 | 100.7 | 15.0 |
| 3. Logistical Infrastructure Project | | | | | | | | |
| Activity 1: Coastal Highway Expansion | 1.0 | 0.7 | 28.8 | 30.2 | 25.2 | 0.0 | 85.9 | |
| Activity 2: Border Crossing Infrastructure | 0.5 | 1.5 | 12.5 | 8.1 | 1.1 | 0.0 | 23.7 | |
| Sub-total | 1.5 | 2.2 | 41.3 | 38.3 | 26.3 | 0.0 | 109.6 | 15.7 |
| 4. Monitoring and Evaluation (M&E) | | | | | | | | |
| Activity 1: Monitoring and Evaluation | 0.4 | 0.5 | 0.8 | 0.5 | 0.7 | 1.4 | 4.3 | |
| Sub-total | 0.4 | 0.5 | 0.8 | 0.5 | 0.7 | 1.4 | 4.3 | 0.0 |
| 5. Program Administration and Oversight | | | | | | | | |
| Activity 1: Program Administration | 3.9 | 3.3 | 3.2 | 3.2 | 3.2 | 3.2 | 20.0 | |
| Sub-total | 3.9 | 3.3 | 3.2 | 3.2 | 3.2 | 3.2 | 20.0 | 7.5 |
| TOTAL ESTIMATED MCC AND GOVERNMENT FUNDING | 10.0 | 22.0 | 76.2 | 75.2 | 71.8 | 21.8 | 277.0 | 88.2 |

ANNEX III

COMPACT MONITORING & EVALUATION SUMMARY

This Annex III summarizes the monitoring and evaluation plan for this Compact (“*M&E Plan*”). The actual structure and content of the M&E Plan, which may differ from those specified in this Annex III, will be agreed to by MCC and the Government in accordance with MCC’s *Policy for Monitoring and Evaluation of Compacts and Threshold Programs* (the “*MCC M&E Policy*”). In addition, the M&E Plan may be modified from time to time as described in the MCC M&E Policy without requiring an amendment to this Annex III. The M&E Plan will be posted publicly on the MCC website and updated as necessary.

1. Objective.

MCC and the Government will formulate and agree to, and the Government will implement or cause to be implemented, an M&E Plan that explains in detail how and what MCC and MCA-El Salvador will (a) monitor to determine whether the Projects are on track to achieve their intended results (“*Monitoring Component*”), and (b) evaluate to assess implementation strategies, provide lessons learned, determine cost effectiveness and estimate the impact of Compact interventions (“*Evaluation Component*”). The M&E Plan will summarize all indicators that must be reported to MCC on a regular basis, as well as a description of any complementary data to be collected for evaluation of programs. The M&E Plan will also include any monitoring and evaluation (“*M&E*”) requirements that MCA-El Salvador must meet in order to receive Disbursements, and will serve as a communication tool so that MCA-El Salvador staff and other stakeholders clearly understand the objectives and targets that MCA-El Salvador is responsible for achieving. The results of M&E activities, measured by monitoring data and evaluations, will be made publicly available on the website of MCA-El Salvador and on the MCC website.

2. Program Logic.

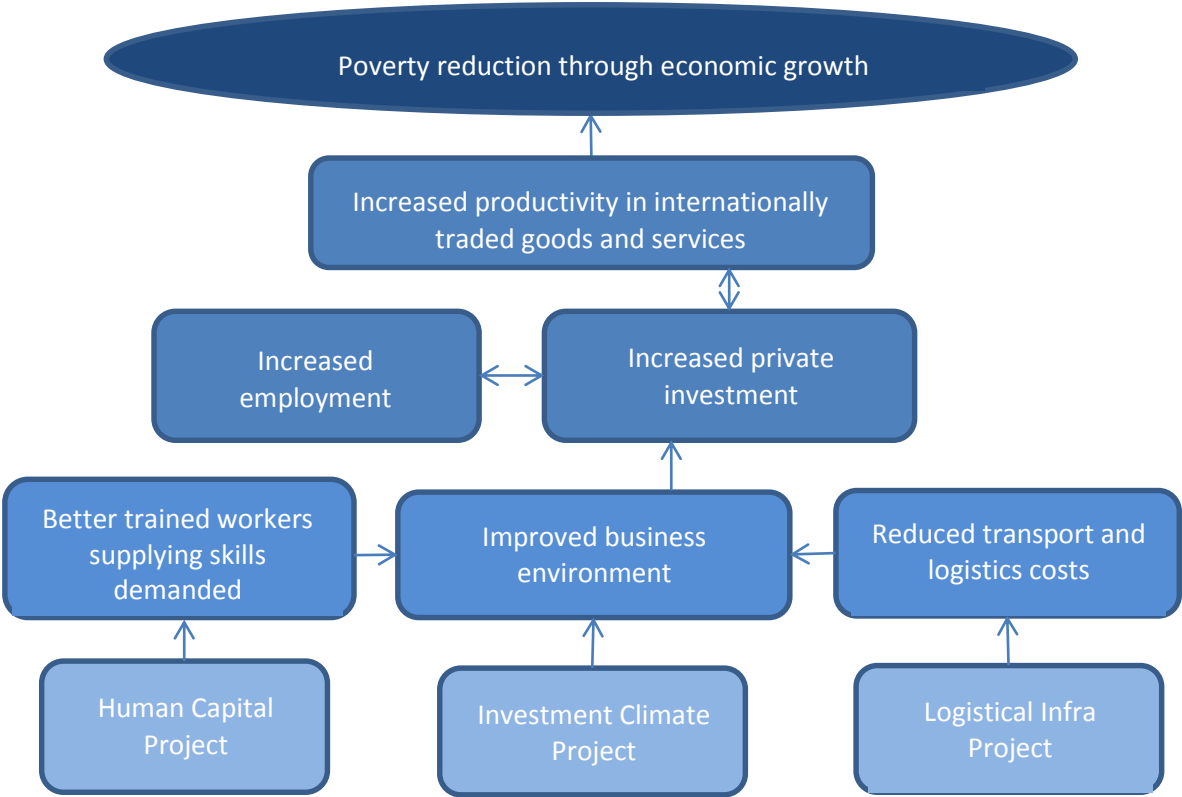
The M&E Plan will summarize the clearly defined compact-level logic model which illustrates how the Projects, Activities, and Sub-Activities (as necessary) contribute to the Compact Goal, Program Objective, and Project Objectives. This higher level logic model will be complemented by lower level logic models at the Project, Activity, and/or Sub-Activity levels (as necessary) depending on Compact design and implementation. All logic models will clearly summarize the outputs, outcomes, and goal expected to result from the Program.

The CA found that El Salvador’s low productivity in trade in international goods and services is a binding constraint to economic growth. In order for El Salvador’s trade in international goods and services to be competitive with world markets, the factors of production in El Salvador must also be competitive with world markets. The total factors of productivity include human capital, physical capital, and often logistics/transportation. The institutional environment can also affect productivity. As a result, the Compact takes a multi-pronged approach to enhance El Salvador’s competitiveness in these factors of productivity.

The Investment Climate Project seeks to increase private investment by improving El Salvador’s regulatory environment and institutional capacity and providing key public services in partnership with the private sector. The Human Capital Project is expected to improve the

quality of education and better match the skills demanded by employers in the international trade of goods and services, thus increasing the labor productivity of future Salvadoran workers. Through the Logistical Infrastructure Project, the Program seeks to reduce logistical and transportation costs to increase investment and productivity in the trade of goods and services.

By improving the business environment, improving the quality of education, and reducing transportation and logistics costs, MCC’s investments are intended to increase the productivity of current firms involved in the trade of international goods and services, which is expected to increase current production (and subsequently, employment). Firms are then expected to invest new revenues in more productive technology to realize greater returns on future production. Through this self-reinforcing feedback loop, higher employment and output, enabled by greater productivity in traded goods and services, are expected over time. A diagram of the logic underlying the compact is included below:



3. Projected Economic Benefits and Beneficiaries.

(a) Investment Climate Project.

Benefits from the Regulatory Improvement Activity of the Investment Climate Project will accrue in the form of variable and fixed cost savings to firms that are affected by the reforms that the Government implements under the Compact. The economic impact of this Activity relies on the implementation of high impact reforms, which should achieve a return of at least 10 per cent. Due to the difficulty of quantifying the impacts of the demonstration and learning effects that result from the Partnership Development Activity, the economic analysis for this Activity assumes no direct benefits beyond net gains to partner firms, the Government, and identified

third parties who derive higher incomes as a result of the ESIC partnerships. The ERR for the ESIC fund is assumed to be 12.5 percent, which is the threshold to qualify for investment under the Compact for an individual ESIC project. The ERRs for the two proposed PPPs are based on the improved operational efficiency and risk management resulting from private management of the two proposed projects.

(b) Human Capital Project.

The Human Capital Project, including both Activities, is expected to contribute to an estimated US\$1.569 billion in benefits for 176,000 beneficiaries in grades 7-12 over a 65-year time horizon.¹ Both the Education Quality Activity and the TVET System Reform Activity are included in a single economic model as beneficiaries are overlapping and the Activities are complementary.

The benefits of the human capital project stem from:

- (i) increased education-years due to reduction in dropout rates in grades 7-12;
- (ii) increased education-years due to greater time-on-task as a result of the full-time inclusive school model;
- (iii) savings from reduced dropout rates in grades 7-12; and
- (iv) increased employment probability for students who achieve high school-level education.

(c) Logistical Infrastructure Project.

The economic analysis for the Logistical Infrastructure Project incorporates assumptions about future expected traffic growth, travel velocity, vehicle operation costs, average passengers per vehicle, and overall travel time to estimate the reduction in vehicle operating costs and travel time that are attributable to each of the proposed Activities. The majority of benefits in the Border Crossing Infrastructure Activity stem from the reduction in wait times to cross the border into Honduras at El Amatillo from 6.1 hours to 0.5 hours on average.

The economic analyses described above generate an expected range of social rates of return or ERRs. The table below summarizes the ERR results of the analyses for each Project proposed in the Compact.

¹ The time horizon includes the 20-year lifespan of the project, plus a 45-year working life of the participants.

| Project/Activity | Estimated ERR Range | ERR Point Estimate ² |
|-----------------------------------|----------------------------|--|
| Investment Climate Project | 15% - 25% | 18.56% |
| Human Capital Project | 8% - 13% | 11.35% |
| Logistical Infrastructure Project | 14% - 23% | 20.31% |

The M&E Plan will also define in detail the persons or entities expected to benefit from the Program. Beneficiary analysis is an extension of economic rate of return analysis that seeks to disaggregate the total increase in income to determine specifically which segments of society will benefit from the proposed Compact activities. MCC considers beneficiaries³ of projects to be those people who experience better standards of living as a result of the project through higher real incomes. The expected beneficiaries of this Compact are shown in the following table:

| Project/Activity | Estimated Beneficiaries |
|-----------------------------------|---|
| Investment Climate Project | Firms operating in El Salvador (up to 25,000) who realize cost savings as a result of Investment Climate Activities |
| Human Capital Project | 176,000 students in grades 7-12 |
| Logistical Infrastructure Project | Individuals and firms using the roads; 171,159 individuals living within 5 kilometers of the proposed construction |

The M&E Plan will also outline key assumptions and risks that underlie the program logic. However, such assumptions and risks will not excuse any Party’s performance unless otherwise expressly agreed to in writing by the other Party. The known assumptions and risks include:

(x) Investment Climate Project.

- *Regulatory Improvement Activity.* The success of the Regulatory Improvement Activity depends on the Government’s commitment to implement and maintain regulatory reforms, despite resistance from parties with vested interests in existing regulations, and the Government’s ability to meaningfully engage with the private sector.
- *Partnership Development Activity.* The success of the Partnership Development Activity depends on the viability of the PPPs, demand for ESIC public investments and the Government’s sustained use of learning gained from the implementation of ESIC in the selection of future, post-Compact public investments.

² ERR Point Estimates are derived from the economic analysis using “base case” parameters that are deemed reasonable at the time of the analysis. Economic and other parameters that the model uses to generate ERR estimates are subject to change as information about the Project changes.

³ As used in this Compact, the term “beneficiary” has the meaning described MCC’s *Guidelines for Economic and Beneficiary Analysis*.

(y) Human Capital Project.

- *Education Quality Activity.* The success of the Education Quality Activity depends on the Government's continued willingness to implement and enforce legal and policy reforms, on-time and within-budget completion of infrastructure works, and MINED's implementation of its O&M Plan.
- *TVET Systems Reform Activity.* The success of the TVET Systems Reform Activity also depends on the Government's continued willingness to implement and enforce legal and policy reforms, private sector participation in industry-based training initiatives and curricula development, and the ability of the TVET system to implement operational reforms.

(z) Logistical Infrastructure Project.

- *Coastal Highway Expansion Activity and Border Crossing Infrastructure Activity.* The success of these Activities depends on the proper management of resettlement and land acquisition of the right of way for the roads, mitigation of construction related risks with adequate health and safety measures, proper plans for risk mitigation addressing trafficking in persons and HIV/AIDS, and sustainable road maintenance by the Government.

4. **Monitoring Component.**

As defined in the MCC M&E Policy, monitoring is the continuous, systematic collection of data on specified indicators to provide indications of progress toward objectives and the achievement of intermediate results along the way. To monitor progress toward the achievement of results of this Compact, the Monitoring Component of the M&E Plan will identify (i) the Indicators (as defined below), (ii) the definitions of the Indicators, (iii) the sources and methods for data collection, (iv) the frequency for data collection, (v) the party or parties responsible for collecting and analyzing relevant data, and (vi) the timeline for reporting on each Indicator to MCC. It should be noted that some Indicators will continue to be tracked after this Compact expires as necessary.

Goal, Outcome, Output, and Process Indicators. The M&E Plan will measure the results of the Program using quantitative, objective, and reliable data ("**Indicators**").

(a) The M&E Plan will establish baselines for every Indicator (each, a "**Baseline**"). An Indicator's Baseline should be established prior to the start of the corresponding Project, Activity and/or Sub-Activity. Baselines demonstrate that the problem can be specified in measurable terms, and are thus a pre-requisite for adequate intervention design. The Government will collect Baselines on the selected Indicators or verify already collected Baselines where applicable.

(b) The M&E Plan will establish a benchmark for each Indicator that specifies the expected value and the expected time by which the result will be achieved ("**Target**").

(c) The M&E Plan will indicate which Indicators will be disaggregated by sex, income level, and age, and beneficiary types to the extent practical and applicable.

(d) MCC's Common Indicators (as described in the MCC M&E Policy) will also be included as relevant. Where MCC Common Indicators have been included in the tables below, the relevant Common Indicator code is included in parentheses after the Indicator name.

(e) Subject to prior written approval from MCC and in accordance with the MCC M&E Policy, the Government may add Indicators or refine the definitions and Targets of existing Indicators.

(f) MCA-El Salvador must report to MCC on monitoring Indicators in the M&E Plan on a quarterly basis using an Indicator Tracking Table (ITT) in the form provided by MCC. No changes to Indicators, Baselines or Targets may be made in the ITT until the changes have been approved in the M&E Plan. Additional guidance on indicator reporting is contained in *MCC's Guidance on Quarterly MCA Disbursement Request and Reporting Package*. In the case that MCA-El Salvador submits a six-month disbursement request, the ITT must still be submitted quarterly.

Key Indicators that can be reported on at least an annual basis will be included in quarterly monitoring Indicator reports, while Indicators that require survey data or a longer time period to track will be tracked for evaluation purposes. The M&E Plan will contain the monitoring Indicators listed in the following tables:

Table 1.1: Investment Climate Project Monitoring Indicators

| Regulatory Improvement Activity | | | | | |
|--|--|--|--------|----------|-----------------------|
| Result | Indicator | Definition | Unit | Baseline | Compact Target |
| Outcome Indicators | | | | | |
| More efficient institutions and regulations | Indicator(s) measuring improved efficiency will be defined based on more detailed implementation plans | TBD | TBD | TBD | TBD |
| Output Indicators | | | | | |
| Investment climate reform unit established and operating | Reforms implemented | Number of reforms implemented under the regulatory improvement Institution | Number | TBD | TBD |
| Process Indicators | | | | | |
| | Legal creation of the regulatory improvement Institution | The creation of the regulatory improvement Institution by law | Date | N/A | End of Compact Year 1 |

| Partnership Development Activity | | | | | |
|---|--|--|------------|----------|----------------|
| Result | Indicator | Definition | Unit | Baseline | Compact Target |
| Outcome Indicators | | | | | |
| Increased private investment from partnerships | Private investment in partnerships | Amount of US dollars in private investments in partnerships either through a formal PPP contract supported by the Project or due to El Salvador Investment Challenge | US Dollars | 0 | 307,000,000 |
| | Investment leverage from El Salvador Investment Challenge | Private to public investment ratio calculated as the US Dollars of private investment compared to US Dollars of public investment in the El Salvador Investment Challenge completed projects | Ratio | N/A | 1:1 |
| Output Indicators | | | | | |
| Stronger institutions involved with partnerships | People trained on PPP skills | People who have received training on PPPs funded by the Project | Number | 0 | TBD |
| Partnerships developed to leverage public finance | Signed PPP contracts | Number of signed PPP contracts supported by the Project | Number | 0 | 2 |
| | Value of El Salvador Investment Challenge Projects completed | Value of Projects in US Dollars (including both public and private projects) completed under the El Salvador Investment Challenge | US Dollars | 0 | 150,000,000 |
| | Government of El Salvador budget committed to El Salvador Investment Challenge | US Dollars committed by the Government of El Salvador to the El Salvador Investment Challenge | US Dollars | 0 | 50,000,000 |

Table 1.2: Human Capital Project Monitoring Indicators

| Education Quality Activity | | | | | | |
|--|--------------|--|------------------------------------|------------|----------------|----|
| Result | Indicator | Definition | Unit | Baseline | Compact Target | |
| Outcome Indicators | | | | | | |
| Improved internal efficiency of education system | Dropout rate | Number of students who no longer attend school in the following year over the total enrollment of the year in a given grade. | 7 th grade | Percentage | 12 | 5 |
| | | | 8 th grade | Percentage | 13 | 5 |
| | | | 9 th grade | Percentage | 27 | 15 |
| | | | 10 th grade - General | Percentage | 23 | 10 |
| | | | 11 th grade - General | Percentage | 20 | 10 |
| | | | 10 th grade - Technical | Percentage | 25 | 10 |
| | | | 11 th grade - Technical | Percentage | 20 | 10 |
| | | | 12 th grade - Technical | Percentage | 15 | 10 |

Education Quality Activity

| Result | Indicator | Definition | Unit | Baseline | Compact Target | |
|--|--|---|------------------------------------|------------|----------------|---|
| | Repetition rate | Number of repeating students enrolled in a grade in a determined year divided by the total enrollment of the year in a given grade. | 7 th grade | Percentage | 6 | 3 |
| | | | 8 th grade | Percentage | 4 | 2 |
| | | | 9 th grade | Percentage | 2 | 1 |
| | | | 10 th grade - General | Percentage | 6 | 3 |
| | | | 11 th grade - General | Percentage | 4 | 2 |
| | | | 10 th grade - Technical | Percentage | 6 | 3 |
| | | | 11 th grade - Technical | Percentage | 4 | 2 |
| | 12 th grade - Technical | Percentage | 2 | 1 | | |
| Promotion rate | Number of passing students divided by the total number of students completing a given school year within the full-time inclusive school model - in grades 7 - 9; 10 - 11 General; 10 - 12 Technical. | 7-9; 10-11 General; 10-12 Technical | Percentage | TBD | TBD | |
| Higher quality management of education system | School Management Committees functioning | Number of School Management Committees functioning in intervened full-time inclusive schools. | Number | 0 | TBD | |
| Functioning full-time inclusive school model | Students participating in MCC-supported education activities (E-6) | The number of students enrolled or participating in MCC-supported educational schooling programs, inclusive of TVET. | Number | 0 | TBD | |
| Increased time on task | Extended hours in schools under the full-time inclusive school model | Average weekly number of hours within full-time inclusive schools offered in addition to existing academic load for students in 7 th - 9 th grade and 10 - 11 General. | Percentage | 0 | 100 | |
| Output Indicators | | | | | | |
| Rehabilitated and equipped full-time inclusive schools | Educational facilities constructed or rehabilitated (E-4) | The number of educational facilities constructed or rehabilitated according to standards stipulated in MCA contracts signed with implementers. | Number | TBD | TBD | |
| | Educational facilities equipped | Number of educational facilities that receive furniture, equipment, educational supplements in support of intervened full-time inclusive school model. | Number | TBD | TBD | |
| Strengthened curriculum, assessment, and pedagogical systems | Legal, financial, and policy reforms adopted to strengthen education quality (E-3) | The number of reforms, <i>or amendments to regulation or norms</i> , adopted by the public sector attributable to compact support that increase the education sector's capacity to improve access, quality, and/ or relevance of education at any level, from primary to post-secondary (e.g., curricula, professional training, student/teacher assessment). | Number | 0 | TBD | |

Education Quality Activity

| Result | Indicator | Definition | Unit | Baseline | Compact Target |
|--------|--|---|------------|----------|----------------|
| | Instructors trained (E-5) | The number of classroom instructors who complete MCC-supported training focused on instructional quality as defined by the compact training activity. | Number | 0 | TBD |
| | Schools, under the full-time inclusive school model, with student records registered | Number of schools intervened with student records registered as a percentage of all schools under the intervened full-time inclusive school model. | Percentage | 0 | 100 |
| | Gender Policy adopted | Gender Policy developed and adopted at MINED. | Number | 0 | 1 |

Process Indicators

| | | | | | |
|--|--|--|--------|-----|-----|
| Organized full-time inclusive school model | Full-time inclusive school model organized | Number of educational systems identified and organized to function under the full-time inclusive school model. Schools are incorporated into the full-time inclusive school model if they meet one of the following conditions: 1. Enrollment has been consolidated among schools for one or more classroom units. 2. One or more teacher's work in various schools. 3. Schools work together in planning educational activities. 4. Students share resources among schools. | Number | TBD | TBD |
|--|--|--|--------|-----|-----|

Technical Vocational Education and Training (TVET) System Reform Activity

| Result | Indicator | Definition | Unit | Baseline | Compact Target |
|--|--|---|--------|----------|----------------|
| Outcome Indicators | | | | | |
| Improved integration between education system and labor market | Certified TVET professors | Teachers that have finished the trainings and have received certification in technical skills demanded by labor market. | Number | 0 | TBD |
| | Students certified in technical competencies | Students that have received a TVET certificate from the TVET governing body in technical skills demanded by labor market. | Number | 0 | TBD |
| Output Indicators | | | | | |
| Developed strategy to integrate market-driven TVET system | Legal, financial, or policy reforms adopted in the TVET sector (E-3) | The number of reforms adopted by the public sector attributable to compact support in the development of an integrated TVET system. | Number | 0 | TBD |
| | National TVET accreditation system established | National TVET accreditation system, of training organizations, established and operational. | Number | 0 | 1 |

Technical Vocational Education and Training (TVET) System Reform Activity

| Result | Indicator | Definition | Unit | Baseline | Compact Target |
|---|--------------------------------------|--|--------|----------|----------------|
| | Labor Market Observatory established | Labor market observatory established and operational. | Number | 0 | 1 |
| Process Indicators | | | | | |
| Developed strategy to integrate market-driven TVET system | Proposal for a TVET System developed | Proposal document for the formation of a TVET System validated and approved. | Number | 0 | 1 |

Table 1.3: Logistical Infrastructure Project Monitoring Indicators

| Result | Indicator | Definition | Unit | Baseline | Compact Target |
|--|---|---|----------------------|---|---|
| Outcome Indicators | | | | | |
| Reduced transportation time and cost in roads connecting key logistical infrastructure | Average time to complete customs requirements for crossing the border | Average time measured from the vehicle arrival at customs first checkpoint to its release and permission to cross the border | Hours | 6.1 | 0.51 |
| | Average annual daily traffic (R-10) | The average number and type of vehicles per day, averaged over different times (day and night) and over different seasons to arrive at an annualized daily average. | Number | A1: Section 1 12,173 Section 2 8,067 Section 3 5,494 A2: 2,367 | A1: Section 1 13,648 Section 2 9,301 Section 3 6,164 A2: 3,165 |
| | Roughness (R-9) | The measure of the roughness of the road surface, in meters of height per kilometer of distance traveled. | Meters per kilometer | A1: 4.68 A2: 4.41 | A1: 2.50 A2: 2.50 |
| Improved road safety | Road traffic fatalities (R-11) | The number of road traffic fatalities per year on roads constructed, rehabilitated or improved with MCC funding. | Number | TBD | N/A |
| Increased road maintenance funding | Annual road maintenance funding for FOVIAL | Annual budget allocation to FOVIAL for road maintenance, excluding any cost of servicing outstanding loans or other indebtedness | US\$ | TBD | TBD |

| Result | Indicator | Definition | Unit | Baseline | Compact Target |
|--|-------------------------------------|---|------------|----------------|-----------------------|
| Output Indicators | | | | | |
| Improved coastal road to the International Airport & Improved road and infrastructure at the El Amatillo border crossing | Kilometers of roads completed (R-8) | The length of roads in kilometers on which construction of new roads or reconstruction, rehabilitation, resurfacing or upgrading of existing roads is complete (certificates handed over and approved). | Kilometers | A1: 0 A2: 0 | A1: 27.17 A2: 5.74 |
| | Border Control Center completed | Completed construction of the control center (including two stations), including buildings, internal access and connecting roads, parking areas, stormwater drainage, potable water supply system, wastewater treatment plant, lighting, and other infrastructure components that may be necessary for the effective functioning of the control center. | Number | 0 | 1 |

5. Evaluation Component.

While good program monitoring is necessary for program management, it is not sufficient for assessing ultimate results. MCC therefore advocates the use of different types of evaluations as complementary tools to better understand the effectiveness of its programs. As defined in the MCC M&E Policy, evaluation is the objective, systematic assessment of a program's design, implementation and results. MCC is committed to making its evaluations as rigorous as warranted in order to understand the causal impacts of its programs on the expected outcomes and to assess cost effectiveness. The Evaluation Component of the M&E Plan may contain three types of evaluation activities as necessary: (i) independent evaluations (impact and/or performance evaluations); (ii) self-evaluation, and (iii) special studies, each of which is further described in the MCC M&E Policy.

(a) Independent Evaluations. According to the MCC M&E Policy, every Project in a Compact must undergo a comprehensive, independent evaluation (impact and/or performance). The Evaluation Component of the M&E Plan will describe the purpose of the evaluation, methodology, timeline, required MCC approvals, and the process for collection and analysis of data for each evaluation. All independent evaluations must be designed and implemented by independent, third-party evaluators. If the Government wishes to engage an evaluator, the engagement will be subject to the prior written approval of MCC. Contract terms must ensure non-biased results and the publication of results.

For each independent evaluation, MCA-El Salvador is expected to review and provide feedback to independent evaluators on the evaluation design reports, evaluation materials (including questionnaires), baseline report (if applicable), and any interim/final reports in order to ensure proposed evaluation activities are feasible, and final evaluation products are technically and factually accurate.

For all evaluations described below, evaluation opportunities will be discussed with the Government once the MCC-contracted evaluators are on-board and more information is available about the design and implementation of each Project.

(i) Investment Climate Project.

(A) Regulatory Improvement Activity.

An independent evaluator will be hired to assess evaluation methodology options. The evaluation will be designed to capture the likely effects of the Activity on the expected outcomes of increasing the efficiency of institutions and regulations as well as improving the business environment.

The M&E Plan is expected to contain the following evaluation Indicators; however the final list of Indicators will be documented in the final evaluation design:

- Perception of business climate, and
- Cost of doing business.

(B) Partnership Development Activity.

(1) PPP Sub-Activity.

The evaluation of this Sub-Activity is expected to be a performance evaluation, using before-after or perhaps cross-country comparisons. However, ways to conduct an impact evaluation through constructing a counterfactual with an interrupted time series (or other methodologies) will be assessed. The evaluation will be designed to capture the likely effects of the Activity on the expected outcomes of increasing the capacity of the Government to build partnerships with the private sector as well as improving companies' perception of the business environment.

The M&E Plan is expected to contain the following evaluation Indicators; however the final list of Indicators will be documented in the final evaluation design:

- Perception of business climate, and
- Private investment in partnerships.

(2) El Salvador Investment Challenge Sub-Activity.

The feasibility of an impact evaluation will depend on a number of factors including the number of projects selected and rejected, measurable and objective selection criteria, and the range of sizes and sectors of the projects. If an impact evaluation is deemed infeasible, a performance evaluation will be conducted for the Sub-Activity. The evaluation will be designed to capture the likely effects of the Activity on the expected outcomes of increasing the capacity of the Government to build partnerships with the private sector and allocate resources more efficiently, increasing employment and exports as a result of those partnerships, as well as improving companies' perception of the business environment. In addition, rigorous impact evaluations of specific projects funded by ESIC will be conducted when they are feasible, cost effective, and the proponent is in agreement with the evaluation design.

The M&E Plan is expected to contain the following evaluation Indicators; however the final list of Indicators will be documented in the final evaluation design:

- Exports;
- Employment;
- Perception of business climate; and
- Private investment in partnerships.

(ii) Human Capital Project.

(A) Education Quality Activity.

(1) Strengthening the National Education System Sub-Activity.

An independent evaluator will be hired to assess evaluation methodology options. The evaluation will be designed to capture the likely effects of the Sub-Activity on the improved efficiency within MINED. However, a performance evaluation of this Sub-Activity will be complicated by the fact that not only are the benefits to the national education system assumed but there are a number of donors that have been and will continue to work with MINED.

The M&E Plan is expected to contain the following evaluation Indicators; however, the final list of Indicators will be documented in the final evaluation design:

- Sustainability of reforms;
- Creation and sustainability of the National Curriculum Evaluation Commission; and
- Creation and sustainability of the school management committees.

(2) Full-time Inclusive School Model Implementation Sub-Activity.

This Sub-Activity is expected to undergo a randomized control trial (RCT), with randomly selected clusters for inclusion in the Sub-Activity from a group of schools eligible for clusters, where outcomes will be rigorously assessed and attributed to MCC investments (clusters: schools grouped together according to spatial proximity and other organizational aspects), unless deemed impractical by both Parties. The potential exists that not all clusters will receive the same treatment as such it may be possible to assess variations of treatment. The development of an evaluation framework will be closely coordinated between MCC and the Government and MINED.

In order to ensure the validity of the Sub-Activity's evaluation methodology, the Government will ensure that:

- a. no school designated as "Control" within the impact evaluation framework will receive Government- or

donor-funded treatment under the implementation of the full-time inclusive school model beyond those expenditures necessary for continuing operations, insomuch as donor-funded interventions are within the control of the Government;

- b. clusters selected for MCC full-time inclusive school model intervention will neither be systematically targeted nor systematically precluded from other Government activities, funding, or support; and
- c. schools designated as “Control” will neither be systematically targeted nor systematically precluded from other Government activities, funding, or support.

The M&E Plan is expected to contain the following evaluation Indicators; however, the final list of Indicators will be documented in the final evaluation design:

- Enrollment rate;
- Student Performance:
 - Promotion rate;
 - Transition rate;
 - Repeat rate;
 - Dropout rate;
 - Over age rate;
 - Students’ standardized test scores (PAESITA, PAES, TIMSS, and/or others); and
- Post-secondary education;
- Employment; and
- Income.

(B) TVET System Reform Activity.

(1) TVET Governance System Sub-Activity.

An independent evaluator will be hired to assess evaluation methodology options. The evaluation will be designed to capture the likely effects of the Sub-Activity on the improved TVET sector.

The M&E Plan is expected to contain the following evaluation Indicators; however, the final list of Indicators will be documented in the final evaluation design:

- Establishment, efficiency and sustainability of the TVET Governing Body;
- Development, implementation and sustainability of market-driven curricula;
- Establishment, efficiency and sustainability of training institutions' accreditation framework;
- Establishment, efficiency and sustainability of teacher and student certification framework;
- Business-demanded skills; and
- Business perception of high school graduate skills.

(2) TVET Continuous Labor Demand Sub-Activity.

An independent evaluator will be hired to assess evaluation methodology options. The evaluation will be designed to capture the likely effects of the Sub-Activity on the continuous assessment of the labor market.

The M&E Plan is expected to contain the following evaluation Indicators; however, the final list of Indicators will be documented in the final evaluation design:

- Establishment, efficiency and sustainability of labor market observatory.

(ii) Logistical Infrastructure Project.

(A) Coastal Highway Expansion Activity.

The evaluation of this Activity is expected to be a performance evaluation, using a well-known model for assessing the results of road improvements. The evaluation will be designed to capture the likely effects of the Activity on usage of the road, vehicle operating costs and travel time. It may be complimented with additional information on safety on the road and users' perception of the improved road.

The M&E Plan is expected to contain the following evaluation Indicators; however the final list of Indicators will be documented in the final evaluation design:

- Vehicle operating costs, and
- Average travel time.

(B) Border Crossing Infrastructure Activity.

The evaluation of this Activity is likely to be a performance evaluation analyzing border crossing times before and after the infrastructure improvements; however it may be possible to construct a

counterfactual using time-series data and comparing the border crossing to other border crossings in El Salvador.

The M&E Plan is expected to contain the following evaluation Indicators; however the final list of Indicators will be documented in the final evaluation design:

- Border crossing time.

(a) Self-Evaluation. Upon completion of the Compact Program, both MCC and MCA-El Salvador will comprehensively assess three fundamental questions: (i) Did the Program meet Compact objectives; (ii) Why did the Compact Program meet or not meet these objectives; and (iii) What lessons can be learned from the implementation experience (both procedural and substantive). MCA-El Salvador staff will draft the Compact Completion Report (CCR) in the last year of compact implementation to evaluate these fundamental questions and other aspects of Compact Program performance. It should be noted that each department will be responsible for drafting its own section to the report for its own activities, subject to cross-departmental review. After MCA-El Salvador staff drafts the CCR, MCC staff, specifically the Country Team, will draft the Completion Process Evaluation Report (CPEER) within six months after the Compact ends to evaluate these same fundamental questions and other aspects of Compact program performance. Similar to the CCR, each division will be responsible for drafting its own section of the report, subject to cross-departmental review.

(b) Special Studies. Plans for conducting special studies will be determined jointly between the Government and MCC before the approval of the M&E Plan. The M&E Plan will identify and make provision for any special studies, *ad hoc* evaluations, and research that may be needed as part of the monitoring and evaluating of this Compact. Either MCC or the Government may request special studies or *ad hoc* evaluations of Projects, Activities, or the Program as a whole prior to the expiration of the Compact Term.

The results of all evaluations will be made publicly available in accordance with the MCC M&E Policy.

6. Data Quality Reviews.

Data Quality Reviews (DQR) are a mechanism to review and analyze the utility, objectivity, and integrity of performance information. DQRs cover (a) quality of data, (b) data collection instruments, (c) survey sampling methodology, (d) data collection procedures, (e) data entry, storage and retrieval processes, (f) data manipulation and analyses, and (g) data dissemination. MCC requires that an independent entity conduct the DQR, such as a local or international specialized firm or research organization, or an individual consultant, depending on the size of the program or project under review. The frequency and timing of data quality reviews must be set forth in the M&E Plan; however MCC may request a DQR at any time. DQRs should be timed to occur before or early enough in the Compact Term that meaningful remedial measures (if any) may be taken depending on the results of the review. The methodology for the review should include a mix of document and record reviews, site visits, key informant interviews, and focus groups.

7. Other Components of the M&E Plan.

In addition to the monitoring and evaluation components, the M&E Plan will include the following components:

(a) Management Information System. The M&E Plan will describe the information system that will be used to collect data, store, process and deliver information to relevant stakeholders in such a way that the Program information collected and verified pursuant to the M&E Plan is at all times accessible and useful to those who wish to use it. The system development will take into consideration the requirement and data needs of the components of the Program, and will be aligned with existing MCC systems, other service providers, and ministries.

(b) Budget. A detailed cost estimate for all components of the M&E Plan.

(c) Responsibility for Developing the M&E Plan.

MCC desires to “[refrain] from requesting the introduction of performance Indicators that are not consistent with countries’ national development strategies.”⁴ For this reason, primary responsibility for developing the M&E Plan lies with the M&E Directorate of MCA-El Salvador with support and input from MCC’s M&E and economist staff. The M&E Plan must be developed in conjunction with key stakeholders, including MCA-El Salvador leadership and sector leads, the MCC Resident Country Mission, and other MCC staff (such as Environmental and Social Performance (ESP) and Social and Gender Assessment (SGA)), as well as external stakeholders, as applicable. While the entire M&E Plan must be developed collaboratively, MCC and MCA-El Salvador Project/Activity leads are expected to guide the selection of Indicators at the process and output levels that are particularly useful for management and oversight of Projects and Activities.

(d) Approval and Implementation of the M&E Plan.

The approval and implementation of the M&E Plan, as amended from time to time, will be in accordance with the Program Implementation Agreement, any other relevant Supplemental Agreement and the MCC M&E Policy. All M&E Plan modifications made by MCA-El Salvador must be submitted to MCC for formal approval. The M&E Plan may undergo peer review within MCC before the beginning of the formal approval process.

(e) Post Compact M&E Plan.

As part of the planning process for winding up the Program at the end of the Compact Term, MCC and MCA-El Salvador will develop a post-Compact M&E Plan designed to observe the persistence of benefits created under the Compact. This plan should describe future monitoring and evaluation activities, identify the individuals and organizations that would undertake these activities, and provide a budget framework for future monitoring and evaluation. The post-Compact M&E Plan should build directly off the Compact M&E Plan.

⁴ Busan Partnership for Effective Development Cooperation, Busan Outcome Document, 1 December 2011, p. 5

ANNEX IV
CONDITIONS PRECEDENT
TO DISBURSEMENT OF COMPACT IMPLEMENTATION FUNDING

This Annex IV sets forth the conditions precedent applicable to Disbursements of Compact Implementation Funding (each a “*CIF Disbursement*”). Upon execution of the Program Implementation Agreement, each CIF Disbursement will be subject to the definitions and terms of the Program Implementation Agreement.

1. Conditions Precedent to Initial CIF Disbursement.

Each of the following must have occurred or been satisfied prior to the initial CIF Disbursement:

- (a) The Government (or MCA-El Salvador) has delivered to MCC:
 - (i) a letter regarding provisional application in accordance with Section 7.5;
 - (ii) an interim fiscal accountability plan acceptable to MCC; and
 - (iii) a CIF procurement plan acceptable to MCC.

2. Conditions Precedent to all CIF Disbursements (Including Initial CIF Disbursement).

Each of the following must have occurred or been satisfied prior to each CIF Disbursement:

- (a) The Government (or MCA-El Salvador) has delivered to MCC the following documents, in form and substance satisfactory to MCC:
 - (i) a completed CIF disbursement request, together with the applicable Periodic Reports, for the applicable CIF Disbursement Period, all in accordance with the Reporting Guidelines (“*CIF Disbursement Request*”);
 - (ii) a certificate of the Government (or MCA-El Salvador), dated as of the date of the CIF Disbursement Request, in such form as provided by MCC;
 - (iii) a certificate of the Fiscal Agent, dated as of the date of the CIF Disbursement Request, in such form as provided by MCC; and
 - (iv) a certificate of the Procurement Director, dated as of the date of the CIF Disbursement Request, in such form as provided by MCC.
- (b) The Bank Agreement remains in full force and effect.
- (c) The Fiscal Agent Agreement remains in full force and effect.
- (d) The Fiscal Oversight Agreement remains in full force and effect.
- (e) MCC is satisfied, in its sole discretion, that (i) the activities being funded with such CIF Disbursement are necessary, advisable or otherwise consistent with the goal of

facilitating the implementation of the Compact and will not violate any applicable law or regulation; (ii) no material default or breach of any covenant, obligation or responsibility by the Government, MCA-El Salvador or any Government entity has occurred and is continuing under this Compact or any Supplemental Agreement; (iii) there has been no violation of, and the use of requested funds for the purposes requested will not violate, the limitations on use or treatment of MCC Funding set forth in Section 2.7 of this Compact or in any applicable law or regulation; (iv) any Taxes paid with MCC Funding through the date 90 days prior to the start of the applicable CIF Disbursement Period have been reimbursed by the Government in full in accordance with Section 2.8(c) of this Compact; and (v) the Government has satisfied all of its payment obligations, including any insurance, indemnification, tax payments or other obligations, and contributed all resources required from it, under this Compact and any Supplemental Agreement.

(f) For any CIF Disbursement occurring after this Compact has entered into force in accordance with Article 7: MCC is satisfied, in its sole discretion, that (i) MCC has received copies of any reports due from any technical consultants (including environmental auditors engaged by MCA-El Salvador) for any Activity since the previous CIF Disbursement Request, and all such reports are in form and substance satisfactory to MCC; (ii) the Implementation Plan Documents and Fiscal Accountability Plan are current and updated and are in form and substance satisfactory to MCC, and there has been progress satisfactory to MCC on the components of the Implementation Plan for any relevant Projects or Activities related to such CIF Disbursement; (iii) there has been progress satisfactory to MCC on the M&E Plan and Social and Gender Integration Plan for the Program or relevant Project or Activity and substantial compliance with the requirements of the M&E Plan and Social and Gender Integration Plan (including the targets set forth therein and any applicable reporting requirements set forth therein for the relevant CIF Disbursement Period); (iv) there has been no material negative finding in any financial audit report delivered in accordance with this Compact and the Audit Plan, for the prior two quarters (or such other period as the Audit Plan may require); (v) MCC does not have grounds for concluding that any matter certified to it in the certificates provided pursuant to paragraph 2(a) of this Annex IV is not as certified; and (vi) if any of the officers or key staff of MCA-El Salvador have been removed or resigned and the position remains vacant, MCA-El Salvador is actively engaged in recruiting a replacement.

(g) MCC has not determined, in its sole discretion, that an act, omission, condition, or event has occurred that would be the basis for MCC to suspend or terminate, in whole or in part, the Compact or MCC Funding in accordance with Section 5.1 of this Compact.

ANNEX V DEFINITIONS

Activity has the meaning provided in Part B of Annex I.

Additional Representative has the meaning provided in Section 4.2.

Audit Guidelines has the meaning provided in Section 3.8(a).

Bank Agreement means that certain Bank Agreement between the Technical and Planning Secretariat of the Presidency, to be replaced by MCA-El Salvador, and Banco Agricola SA, dated June 12, 2013.

Baseline has the meaning provided in paragraph 4(a) of Annex III.

Board of Directors has the meaning provided in paragraph 1(a) of Part C of Annex I.

CA has the meaning provided in paragraph 1(a) of Part A of Annex I.

CA-2 has the meaning provided in paragraph 3(a)(i) of Part B of Annex I.

CAFTA-DR has the meaning provided in paragraph 1(a) of Part A of Annex I.

CIF Disbursement has the meaning provided in Annex IV.

CIF Disbursement Period means the quarter for which a CIF Disbursement has been requested, or such other period of time as agreed by MCC.

CIF Disbursement Request has the meaning provided in paragraph 2(a)(i) of Annex IV.

Compact has the meaning provided in the Preamble.

Compact Goal has the meaning provided in Section 1.1.

Compact Implementation Funding has the meaning provided in Section 2.2(a).

Compact Records has the meaning provided in Section 3.7(a).

Compact Term has the meaning provided in Section 7.4.

Covered Provider has the meaning provided in the Audit Guidelines.

DF has the meaning provided in paragraph 3(a) of Part C of Annex I.

Disbursement has the meaning provided in Section 2.4.

El Salvador has the meaning provided in the Preamble.

ERR means economic rate of return.

ESA has the meaning provided in paragraph 2(c) of Part B of Annex I.

ESIA has the meaning provided in paragraph 1(c) of Part B of Annex I.

ESIC has the meaning provided in paragraph 1(a)(ii) of Part B of Annex I.

ESIC Operations Manual has the meaning provided in paragraph 1(a)(ii) of Part B of Annex I.

ESMF has the meaning provided in paragraph 2(c) of Part B of Annex I.

ESMS has the meaning provided in paragraph 3 of Part A of Annex I.

Evaluation Component has the meaning provided in paragraph 1 of Annex III.

Excess CIF Amount has the meaning provided in Section 2.2(d).

Fiscal Agent has the meaning provided in paragraph 3(a) of Part C of Annex I.

Fiscal Agent Agreement has the meaning provided in paragraph 3(a) of Part C of Annex I.

Fiscal Oversight Agent has the meaning provided in paragraph 3(b) of Part C of Annex I.

Fiscal Oversight Agreement has the meaning provided in paragraph 3(b) of Part C of Annex I.

FOVIAL has the meaning provided in paragraph 3(a)(i) of Part B of Annex I.

Governance Guidelines means MCC's Guidelines for Accountable Entities and Implementation Structures, as such may be posted on MCC's Website from time to time.

Government has the meaning provided in the Preamble.

Government Contribution has the meaning provided in paragraph 2 of Annex II.

Grant has the meaning provided in Section 3.6(b).

Growth Council has the meaning provided in paragraph 1(a) of Part A of Annex I.

IDB has the meaning provided in paragraph 3(d) of Part B of Annex I.

IFC Performance Standards has the meaning provided in paragraph 3 of Part A of Annex I.

Implementation Letter has the meaning provided in Section 3.5.

Implementing Entity has the meaning provided in paragraph 2 of Part C of Annex I.

Implementing Entity Agreement has the meaning provided in paragraph 2 of Part C of Annex I.

Indicators has the meaning provided in paragraph 4 of Annex III.

Inspector General has the meaning provided in Section 3.7(c).

Institution has the meaning provided paragraph 1(a)(i) of Part B of Annex I.

Intellectual Property means all registered and unregistered trademarks, service marks, logos, names, trade names and all other trademark rights; all registered and unregistered copyrights; all patents, inventions, shop rights, know how, trade secrets, designs, drawings, art work, plans, prints, manuals, computer files, computer software, hard copy files, catalogues, specifications, and other proprietary

technology and similar information; and all registrations for, and applications for registration of, any of the foregoing, that are financed, in whole or in part, using MCC Funding.

***JCAP** has the meaning provided in paragraph 1(a) of Part A of Annex I.*

***M&E** has the meaning provided in paragraph 1 of Annex III.*

***M&E Plan** has the meaning provided in Annex III.*

***Management Team** has the meaning provided in paragraph 1(c) of Part C of Annex I.*

***MCA Act** has the meaning provided in Section 2.2(a).*

***MCA-El Salvador** has the meaning provided in Section 3.2(b)(i).*

***MCC** has the meaning provided in the Preamble.*

***MCC Environmental Guidelines** has the meaning provided in Section 2.7(c).*

***MCC Funding** has the meaning provided in Section 2.3.*

***MCC Gender Policy** means the MCC Gender Policy (including any guidance documents issued in connection with the guidelines) posted from time to time on the MCC Website or otherwise made available to the Government.*

***MCC M&E Policy** has the meaning provided in Annex III.*

***MCC Program Procurement Guidelines** has the meaning provided in Section 3.6(a).*

***MCC Website** has the meaning provided in Section 2.7.*

***MINED** has the meaning provided in paragraph 2(a)(i) of Part B of Annex I.*

***Monitoring Component** has the meaning provided in paragraph 1 of Annex III.*

***MOP** has the meaning provided in paragraph 3(c) of Part B of Annex I.*

***Multi-Year Financial Plan Summary** has the meaning provided in paragraph 1 of Annex II.*

***O&M** has the meaning provided in paragraph 2(c) of Part B of Annex I.*

***O&M Plan** has the meaning provided in paragraph 2(g) of Part B of Annex I.*

***Party** and **Parties** have the meaning provided in the Preamble.*

***Permitted Account** has the meaning provided in Section 2.4.*

***PfG** has the meaning provided in paragraph 1(a) of Part A of Annex I.*

***PPP Law** has the meaning provided in paragraph 1(a)(ii) of Part B of Annex I.*

***PPPs** has the meaning provided in paragraph 1(a)(ii) of Part B of Annex I.*

Principal Representative has the meaning provided in Section 4.2.

Procurement Director has the meaning provided in paragraph 4 of Part C of Annex I.

Program has the meaning provided in the Recitals.

Program Assets means any assets, goods or property (real, tangible or intangible) purchased or financed in whole or in part (directly or indirectly) by MCC Funding.

Program Funding has the meaning provided in Section 2.1.

Program Guidelines means collectively the Audit Guidelines, the MCC Environmental Guidelines, the MCC Gender Policy, the Governance Guidelines, the MCC Program Procurement Guidelines, the Reporting Guidelines, the MCC M&E Policy, the MCC Cost Principles for Government Affiliates Involved in Compact Implementation, the MCC Program Closure Guidelines (including any successor to any of the foregoing) and any other guidelines, policies or guidance papers relating to the administration of MCC-funded compact programs and as from time to time published on the MCC Website.

Program Implementation Agreement and **PIA** have the meaning provided in Section 3.1.

Program Objective has the meaning provided in Section 1.2.

Project(s) has the meaning provided in Section 1.2.

Project Objective(s) has the meaning provided in Section 1.3.

Provider means (a) any entity of the Government that receives or uses MCC Funding or any other Program Asset in carrying out activities in furtherance of this Compact or (b) any third party that receives at least US\$50,000 in the aggregate of MCC Funding (other than as salary or compensation as an employee of an entity of the Government) during the Compact Term.

RAPs has the meaning provided in paragraph 3 of Part A of Annex I.

Reporting Guidelines means the MCC Guidance on Quarterly MCA Disbursement Request and Reporting Package posted by MCC on the MCC Website or otherwise publicly made available.

Road Maintenance Study has the meaning provided in paragraph 3(g) of Part B of Annex I.

SAL has the meaning provided in paragraph 1(a)(ii) of Part B of Annex I.

SEA has the meaning provided in paragraph 3(c) of Part B of Annex I.

Social and Gender Integration Plan has the meaning provided in paragraph 3 of Part A of Annex I.

Stakeholders' Committee has the meaning provided in paragraph 1(d)(i) of Part C of Annex I.

Strategic RAP has the meaning provided in paragraph 3 of Part A of Annex I.

Supplemental Agreement means any agreement between (a) the Government (or any Government affiliate, including MCA-El Salvador) and MCC (including, but not limited to, the PIA), or (b) MCC and/or the Government (or any Government affiliate, including MCA-El Salvador), on the one hand, and any third party, on the other hand, including any of the Providers, in each case, setting forth the details of

any funding, implementing or other arrangements in furtherance of, and in compliance with, this Compact.

***Target** has the meaning provided in paragraph 4(b) of Annex III.*

***Taxes** has the meaning provided in Section 2.8(a).*

***TIP** has the meaning provided in paragraph 3(c) of Part B of Annex I.*

***TVET** has the meaning provided in paragraph 2(a) of Part B of Annex I.*

***TVET Governing Body** has the meaning provided in paragraph 2(a)(ii) of Part B of Annex I.*

***United States Dollars** or **US\$** means the lawful currency of the United States of America.*

***USAID** has the meaning provided in paragraph 1(e) of Part B of Annex I.*

***USG** means the Government of the United States of America.*