



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 Government of Nepal on September 14, 2017 (the “Compact”). We have included a detailed summary of the Compact and a copy of the text of the Compact.

The attached notification is being sent to Congress on September 19, 2017.

In addition, we will provide a link to the Compact and a summary of it in the Federal Register and on MCC’s website.

If you or your staff would like to arrange a meeting to discuss the Compact, please contact Dan Chaison at (202) 521-3593 or chaisondm@mcc.gov.

Sincerely,

/s/

Chris Dunn
Chief of Staff (Acting)
Office of the Chief Executive Officer

Enclosure:
As stated

**MILLENNIUM CHALLENGE CORPORATION
CONGRESSIONAL NOTIFICATION**

September 19, 2017

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 Government of Nepal under section 605 of the Act on September 14, 2017 (the “Compact”). A detailed summary of the Compact and a copy of the text of the Compact follow.

SUMMARY OF THE NEPAL COMPACT

Overview of MCC Nepal Compact

MCC's Board of Directors has approved a five-year, \$500 million compact with Nepal aimed at reducing poverty through economic growth. The compact seeks to assist Nepal in addressing two binding constraints to economic growth: (i) inadequate supply of electricity; and (ii) high cost of transportation. The compact will address these binding constraints by investing in two projects: the Electricity Transmission Project and the Road Maintenance Project.

Background and Context

Nepal's economic growth, labor productivity, and gross domestic product per capita are among the lowest in South Asia. A decade of civil and political unrest from 1996 to 2006 continues to shape the social, economic, and political landscape of the country. The people of Nepal continue to deal with the fallout from a series of devastating earthquakes in 2015 that killed nearly 9,000 people and pushed an additional million below the poverty line. Almost half a million people leave the country each year for economic opportunities elsewhere. In September 2017, Nepal will hold the final phase of a three-phase local, democratic election in hundreds of municipalities throughout the country. These local elections are the first in 20 years and the first to be held since Nepal ratified its constitution in 2015, a critical step in continuing to foster transparency and accountability in government.

The proposed compact is designed to address the underlying causes of two binding constraints to Nepal's growth: inadequate supply of electricity and high cost of transportation. Nepal suffers from the worst electricity shortages in South Asia, and new investment in Nepal's electricity sector is critical to achieve economic growth. Only half of the demand for electricity can be met by the nation's grid, which has resulted in load-shedding of up to 18 hours a day during the dry winter months when hydropower generation is low. The constraints to growth analysis found that the low availability of electricity creates significant costs for businesses that must run generators on expensive imported fuel. The availability of electricity is further reduced by Nepal's constrained ability to import power when needed and the high level of losses in transmission and distribution system.

The transportation sector has also suffered from Nepal's past political instability, inadequate investment, weak planning, and poor project execution. These factors have contributed to poor road quality, inefficient customs and border enforcement, an inefficient trucking industry, and inadequate road coverage. The Government of Nepal recognizes that investments in this sector are needed to reduce transportation costs and promote economic growth.

Compact Overview and Budget

After MCC selected Nepal as eligible for threshold program assistance in December 2011, MCC and the Government of Nepal conducted a constraints to growth analysis. When MCC's Board of Directors selected Nepal as eligible to develop a compact in December 2014, MCC and the Government of Nepal used the analysis completed for the threshold program to develop the proposed compact.

MCC and Nepal identified four binding constraints and agreed to focus the proposed compact on the two best suited for MCC's assistance: the inadequate supply of electricity and the high cost of transportation. The proposed compact seeks to address the selected constraints by investing in two projects: the Electricity Transmission Project and the Road Maintenance Project.

Nepal is already undertaking significant investments in the generation and distribution portions of the power sector value chain. The proposed Electricity Transmission Project therefore seeks to strengthen the transmission portion of the value chain, which has been weakened by historic underinvestment and poor implementation. The Electricity Transmission Project plans to add approximately 300 kilometers to the high-voltage transmission backbone inside Nepal, complete the Nepal portion of the second cross-border transmission line with India for increased electricity trade, and provide technical assistance aimed at improving the sustainability of Nepal's power sector. The compact will also support Nepal's establishment of an independent and capable power sector regulator, which is essential for maintaining open, non-discriminatory access to a transmission network with transparent pricing and clear rules of engagement.

The Road Maintenance Project focuses on improving Nepal's road maintenance regime by providing technical assistance to key actors within the transportation sector. The Road Maintenance Project also includes an incentive-matching fund to encourage the expansion of Nepal's road maintenance budget, in addition to the periodic maintenance of up to 305 kilometers of the country's strategic road network.

The following summary describes the components of Nepal's compact. The MCC investment for the compact is \$500 million, with an additional \$130 million committed by Nepal to support the compact program.

Nepal Compact Budget

Component	Total (Millions \$)
1. Electricity Transmission Project	398.2
1.1 Transmission Lines Activity	228.2
1.2 Substation Activity	114.0
1.3 Power Sector Technical Assistance Activity	22.4
1.4 Project Management Activity	33.6
2. Roads Maintenance Project	52.3
2.1 Technical Assistance Road Maintenance Reform	7.1
2.2 Strategic Road Maintenance Works	45.2
3. Monitoring and Evaluation	9.5
3.1 Monitoring and Evaluation Activities	9.5
4. Program Administration and Oversight	40.0
4.1 MCA-Nepal Program Administration	23.4
4.2 Fiscal Agent, Procurement Agent, Audit	16.6
Total MCC Contribution	500.0
Government of Nepal Contribution	130.0
Total Program Investment	630.0

Project Summaries

The Electricity Transmission Project: The objective of this project is to spur economic activity and growth by improving the availability and reliability of electricity supply in Nepal's power grid, thus increasing per capita electricity consumption. This project includes four activities:

- **Transmission Lines Activity.** This activity will focus on the construction of an estimated 300 kilometers of high voltage transmission lines in Nepal, providing a vital missing link to the existing high voltage grid. Most of the proposed transmission lines traverse mountainous terrain, starting near the Kathmandu Valley, moving to the west and then southwest to the Indian border. The particular lines were selected following careful analyses and feasibility studies that weighed their technical and economic merit, their importance in meeting Nepal's medium and long term electricity supply goals, and their consistency with Nepal's domestic and cross border transmission investment plans. The transmission line route was selected to minimize impact on people and sensitive geographic areas, to the extent possible. Moreover, the activity includes funding for certain community benefit-sharing activities in order to further mitigate potential social impacts from construction of the transmission lines. Potential activities include rural electrification through off-grid solutions and community empowerment programs.

- Substations Activity. This activity is complementary to the Transmission Lines Activity. The proposed compact contemplates constructing three substations. In combination with the transmission lines, these substations would help evacuate and transmit power collected from three major river basins where large hydropower projects are under construction by investors, many of which are private. The substation near Butwal would be the starting point for the transmission line to the Indian border and power grid.
- Power Sector Technical Assistance Activity. This activity seeks to strengthen the proposed power sector regulator (Electricity Regulatory Commission) to help bring transparency, efficiency, and competition to the power sector. The activity would help Nepal embed experts within the Electricity Regulatory Commission to improve the skills of this nascent agency in areas such as rule-making, dispute resolution, and economic and technical regulation. This activity would also help the Nepal Electricity Authority improve its transmission operations and prepare for oversight from the new independent electricity regulator. This will help establish a regulatory cost recovery system, improved grid operations, and better power system planning within the Nepal Electricity Authority.
- Program Management and Technical Oversight Activity. This activity is designed to complement the Transmission Lines and Substation Activities by supporting project management, environmental and social impact assessment, and engineering and technical supervision. This will allow the compact to properly implement the proposed infrastructure investments while complying with MCC's technical, environmental, and social standards.

The Road Maintenance Project: The objective of this project is to avoid future increases in transportation costs across Nepal's road network by preventing further deterioration of maintained roads and to improve the administration of road maintenance. This project has two activities:

- Technical Assistance Activity. This activity is planned to build capacity for the Department of Roads and Roads Board Nepal in (1) improved data collection; (2) preparation of appropriate road maintenance plans and cost estimates; (3) improved prioritization of periodic maintenance; (4) improved contracting and contracting management; and (5) improved project management.
- Strategic Road Maintenance Works Activity. This activity seeks to complement and build upon the Technical Assistance Activity by incentivizing additional government spending on road maintenance. The activity would establish a matching fund to provide \$2 for every \$1 Nepal spends above its current average annual amount for road maintenance, up to a total of \$15 million annually for three years. The activity would additionally provide for the physical maintenance of an initial 305 kilometers out of the 2,000 kilometers of Nepal's strategic road network.

Economic Analysis

The proposed Electricity Transmission Project has an estimated economic rate of return of 12 percent. The investment in Nepal's transmission system is expected to affect all grid-connected consumers, which represent 72 percent of Nepali households. With a projected population in 2024

of 31.5 million people, an estimated 23 million individual beneficiaries living in five million households are expected to benefit from this project. Fifty-two percent of the potential beneficiaries are estimated to be female.

The estimated economic rate of return for the Road Maintenance Project is 29 percent. The 305 kilometers of roads proposed by Nepal for periodic maintenance under the compact are spread across five road segments in five geographic areas. The Project is expected to benefit approximately 924,000 people in 205,000 households.

MCC anticipates that there will be overlap in the beneficiaries of the two proposed projects and thus ultimately expects the compact to benefit approximately 23 million individuals.

Policy Reforms and the Compact

MCC will require certain conditions to entry into force of the compact in order to ensure sustainability of compact investments. For example, given the proposed compact's focus and the clear need for a second cross-border transmission connection with India, MCC will require that technical and financial arrangements for the construction of the complementary investment in India be finalized before entry into force of the compact. This requirement is expected to be further strengthened through conditions regarding the Nepal portion of the cross-border transmission line that must be met for certain compact disbursements.

The proposed compact includes several key reform elements, supported by technical assistance activities in each project. The Power Sector Technical Assistance Activity includes conditions to help Nepal create a transparent and efficient electricity market. MCC believes that the establishment of the Electricity Regulatory Commission as an independent and capable regulator is essential for maintaining open, non-discriminatory access to a transmission network with transparent pricing and clear rules of engagement for all power market participants, particularly investors in generation projects. The compact proposes to increase the utility's planning, operations, and cost recovery mechanisms to help ensure the sustainability of the proposed investments. Strengthening the utility's transmission operations should ensure its viability if Nepal decides to spin off or merge those operations with an independent transmission company. MCC has conditioned the entry into force of the compact on satisfactory progress toward parliamentary approval of a bill to establish the Electricity Regulatory Commission. Further, funding for the Power Sector Technical Assistance Activity will only be provided if the Electricity Regulatory Commission bill has been passed by the Nepali parliament.

For the Technical Assistance Activity in the Road Maintenance Project, MCC will provide compact funding for maintenance works only if Nepal increases its own historically low spending levels on road maintenance. The compact is expected to incentivize Nepal to increase its spending for road maintenance significantly by making MCC funding conditioned on increased Nepal spending.

MILLENNIUM CHALLENGE COMPACT

BETWEEN

**THE UNITED STATES OF AMERICA
ACTING THROUGH
THE MILLENNIUM CHALLENGE CORPORATION**

AND

**THE FEDERAL DEMOCRATIC REPUBLIC OF NEPAL
ACTING THROUGH
THE MINISTRY OF FINANCE**

MILLENNIUM CHALLENGE COMPACT
TABLE OF CONTENTS

	<u>Page</u>
ARTICLE 1. GOAL AND OBJECTIVES	1
Section 1.1 Compact Goal	1
Section 1.2 Project Objectives	1
ARTICLE 2. FUNDING AND RESOURCES	2
Section 2.1 Program Funding	2
Section 2.2 Compact CDF	2
Section 2.3 MCC Funding	3
Section 2.4 Disbursement	3
Section 2.5 Interest.....	3
Section 2.6 Government Resources; Budget	3
Section 2.7 Limitations on the Use of MCC Funding	3
Section 2.8 Taxes	4
ARTICLE 3. IMPLEMENTATION	5
Section 3.1 Program Implementation Agreement.....	5
Section 3.2 Government Responsibilities	5
Section 3.3 Policy Performance.....	6
Section 3.4 Accuracy of Information.....	6
Section 3.5 Implementation Letters	6
Section 3.6 Procurement and Grants.....	6
Section 3.7 Records; Accounting; Covered Providers; Access	7
Section 3.8 Audits; Reviews	7
ARTICLE 4. COMMUNICATIONS	8
Section 4.1 Communications	8
Section 4.2 Representatives	9
Section 4.3 Signatures.....	9
ARTICLE 5. TERMINATION; SUSPENSION; EXPIRATION.....	10
Section 5.1 Termination; Suspension	10
Section 5.2 Consequences of Termination, Suspension, or Expiration	10
Section 5.3 Refunds; Violation	11

Section 5.4	Late Payment Interest	11
Section 5.5	Survival	11
ARTICLE 6. COMPACT ANNEXES; AMENDMENTS; GOVERNING LAW.....		11
Section 6.1	Annexes.....	11
Section 6.2	Amendments and Modifications	12
Section 6.3	Inconsistencies	12
Section 6.4	Governing Law	12
Section 6.5	Additional Instruments.....	12
Section 6.6	References to MCC Website.....	12
Section 6.7	References to Laws, Regulations, Policies, and Guidelines, References to Compact Expiration and Termination.....	13
Section 6.8	MCC Status.....	13
ARTICLE 7. ENTRY INTO FORCE.....		13
Section 7.1	Domestic Requirements	13
Section 7.2	Conditions Precedent to Entry into Force	13
Section 7.3	Date of Entry into Force	14
Section 7.4	Compact Term	14
Section 7.5	Provisional Application	14
ARTICLE 8. ADDITIONAL GOVERNMENT COVENANTS.....		14
Section 8.1	Covenant for the Electricity Transmission Project	14
<u>Annex I:</u>	Program Description	
<u>Annex II:</u>	Multi-Year Financial Plan Summary	
<u>Annex III:</u>	Compact Monitoring & Evaluation Summary	
<u>Annex IV:</u>	Conditions to Disbursement of Compact CDF	
<u>Annex V:</u>	Additional Conditions Precedent to Entry Into Force	
<u>Annex VI:</u>	Definitions	
<u>Annex VII:</u>	Tax Schedules	

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 Federal Democratic Republic of Nepal (“*Nepal*”), acting through its Ministry of Finance (the “*Government*”) (individually, a “*Party*” and collectively, the “*Parties*”). Capitalized terms used in this Compact will have the meanings provided in Annex VI.

Recognizing that the Parties are committed to the shared goals of promoting economic growth and the elimination of poverty in Nepal and that MCC assistance under this Compact supports Nepal’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 Nepal 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 Nepal implement the program described herein to achieve the goal and objectives described herein (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 Nepal (the “*Compact Goal*”). MCC’s assistance will be provided in a manner that strengthens good governance, economic freedom, and investments in the people of Nepal.

Section 1.2 Project Objectives. The Program consists of the projects described in Annex I (each a “*Project*” and collectively, the “*Projects*”). The objective of each of the Projects (each a “*Project Objective*” and collectively, the “*Project Objectives*”) is to:

- (a) Increase electricity consumption by facilitating power trade and by improving the availability and reliability of electricity supply in Nepal’s electricity grid; and by facilitating power trade, and
- (b) Maintain road quality across the strategic road network.

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 Four Hundred Fifty-Nine Million Five Hundred Thousand United States Dollars (US\$459,500,000) (“**Program Funding**”) for use by the Government to implement the Program. The allocation of Program Funding is generally described in Annex II.

Section 2.2 Compact CDF.

(a) Upon the signing of this Compact, 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 Forty Million Five Hundred Thousand United States Dollars (US\$40,500,000) (“**Compact CDF**”) 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 this Compact, including for the following purposes:

- (i) financial management and procurement activities;
- (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 and activities; and
- (v) other activities to facilitate Compact implementation as approved by MCC.

The allocation of Compact CDF 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 CDF will be effective, for purposes of Compact CDF only, as of the date this Compact is signed by MCC and the Government.

(c) Each Disbursement of Compact CDF 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 CDF 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 CDF available under Section 2.2(a) (such excess, the “**Excess Compact CDF Amount**”). In such event, the amount of Compact CDF granted to the Government under Section 2.2(a) will be reduced by the Excess Compact CDF Amount, and MCC will have no further obligations with respect to such Excess Compact CDF 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 Compact CDF 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 CDF are collectively referred to in this Compact as “**MCC Funding**,” and includes any refunds or reimbursements of Program Funding or Compact CDF 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, MCC will make the proceeds of Disbursements available to the Government either 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) 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. In addition, the Government will make a contribution towards meeting the Project Objectives of this Compact (“**Government Contribution**”). Annex II describes the Government Contribution in more detail.

(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 accounted for in its annual budget 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, 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 such guidelines (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 is free from the payment or imposition of any existing or future taxes, duties, levies, contributions or other similar charges (but not fees or charges for services that are generally applicable in Nepal, reasonable in amount and imposed on a non-discriminatory basis) ("*Taxes*") of or in Nepal (including any such Taxes imposed by a national, federal, state, local, or other governmental or taxing authority of or in Nepal). Specifically, and without limiting the generality of the foregoing, MCC Funding will be free from the payment of (i) any tariffs, customs duties, import taxes, export taxes, and other similar charges on any goods, works or services introduced into Nepal in connection with the Program; (ii) value added tax, sales tax, excise duty, property transfer tax, and other similar charges on any transactions involving goods, works or services in connection with the Program, (iii) taxes and other similar charges on ownership, possession or use of any property in connection with the Program, and (iv) taxes and other similar charges on income, profits or gross receipts attributable to work performed in connection with the Program and related social security taxes and other similar charges on all natural or legal persons performing work in connection with the Program except (1) natural persons who are citizens or permanent residents of Nepal and (2) legal persons formed under the laws of Nepal (but excluding MCA-Nepal and any other entity formed for the purpose of implementing the Government's obligations hereunder).

(b) The mechanisms that the Government will use to implement the tax exemption required by Section 2.8(a) for certain principal taxes are set forth in Annex VII. 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-Nepal or to the taxpayer, or payment by the Government to MCA-Nepal 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 Annex VII, 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 Nepal within 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-Nepal) that such Tax has been paid. Failure to refund such amount within the specified time will result in interest accruing on the unpaid amount in accordance with Section 5.4.

(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).

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) With the prior written consent of MCC, the Government will designate an entity to be established through a formation order issued by the Council of Ministers of Nepal, 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-Nepal*,” and will have the authority to act on behalf of the Government with regard to all Program activities. The Government hereby also designates MCA-Nepal to exercise and perform the Government’s rights and responsibilities to oversee, manage, and implement the activities defined in the Amended and Restated Initial Engagement Technical Assistance Grant Agreement, dated July 20, 2016. The designation contemplated by this Section 3.2(b) 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).

(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 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, each 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 advise 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 advice in implementing the Program. The Parties may also issue jointly agreed-upon Implementation Letters to confirm and record their mutual understanding on aspects related to the implementation of this Compact, the PIA, or other related agreements.

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 MCC's *Program Procurement Guidelines* (the "**MCC Program Procurement Guidelines**"). 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-Nepal 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 Nepal. Compact Records must be maintained for at least five 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 at least a semi-annual basis, conduct, or cause to be conducted, financial audits of all disbursements of MCC Funding covering the period from signing of this Compact until the earlier of the following September 30 or March 31 and covering each six-month period thereafter ending September 30 and March 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 MCC’s Guidelines for Financial Audits Contracted by the Millennium Challenge Corporation’s Accountable Entities issued and revised from time to time by the Inspector General (the “*Audit Guidelines*”). 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. The requirements of this Section 3.8(a) do not preclude the Office of the Auditor General of Nepal from conducting audits of MCA-Nepal.

(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 the Uniform Administrative Requirements, Cost Principles and Audit Requirements for Federal Awards, 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.

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. 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)
1099 Fourteenth Street NW
Washington, DC 20005
United States of America
Facsimile: +1 (202) 521-3700
Telephone: +1 (202) 521-3600
Email: VPOperations@mcc.gov (Vice President, Compact Operations)
VPGeneralCounsel@mcc.gov (Vice President and General Counsel)

To the Government:

Ministry of Finance
Attention: Finance Secretary
(With a copy to the Joint Secretary, International Economic Cooperation
Coordination Division)
Singh Durbar
Kathmandu
Nepal
Facsimile: +977-1-4211161
Telephone: +977-1-4211164
Email: secretary@mof.gov.np

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, the Minister of Finance of the Federal Democratic Republic of Nepal, 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). The Government hereby designates the future Executive Director of MCA-Nepal as an Additional Representative. MCC hereby designates the Deputy Vice President, Department of Compact Operations, Europe, Asia, Pacific, and Latin America 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.

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 30 days' prior written notice. MCC may also terminate this Compact or MCC Funding without cause in part by giving the Government 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 to the Government in writing) 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 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 Nepal 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 Nepal for assistance under the MCA Act; and

(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) The Parties agree that they will endeavor in good faith to consult the other Party in the event of a termination under Section 5.1(a).

(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.

(c) 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.

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 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 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 unpaid amount at a rate equal to 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 paid in full. Any such payment will first be credited against interest due, and once the interest due amount is extinguished, then payments will be credited against outstanding principal.

Section 5.5 Survival. The Government's responsibilities under this Section 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, provided that the terms of Section 2.8 will survive for only 120 days following this Compact's expiration.

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 agreement will specify how it enters into force.

(b) Notwithstanding subsection (a) the Parties agree that the Government and MCC may by written agreement, which will enter into force upon signature, modify any Annex to (i) suspend, terminate or modify any Project or Activity, (ii) change the allocations of funds as set forth in Annex II, (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 III in accordance with the MCC M&E Policy, (v) add, delete or waive any condition precedent described in Annex IV or (vi) modify the mechanisms for exempting MCC Funding from Taxes as set forth in Annex VII; provided that, in each case, any such modification (1) is consistent in all material respects with the Project Objectives, (2) 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)), (3) does not cause the amount of Compact CDF to exceed the aggregate amount specified in Section 2.2(a), (4) does not reduce the Government's responsibilities or contribution of resources required under Section 2.6(a), and (5) does not extend the Compact Term.

(c) The Parties understand that any modification of any Annex pursuant to Section 6.2(b) may be entered into by the Government without the need for further action by the Government (including any parliamentary action), or satisfaction of any additional domestic requirements of Nepal.

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

(a) any Annex and any of Articles 1 through 8, such Articles 1 through 8, 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, References to Compact Expiration and Termination.

(a) 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.

(b) Each reference in this Compact, the PIA or any other agreement entered into in connection with this Compact, to the Compact's "expiration" refers to the date on which the Compact Terms ends if the Compact is not terminated earlier, which in accordance with Section 7.4 is five years after its entry into force. Each reference in any of the aforementioned documents to the Compact's "termination" refers to the Compact ceasing to be in force prior to its expiration in accordance with Section 5.1.

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 Nepal for any claim or loss arising out of activities or omissions under this Compact.

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. The Parties understand that this Compact, upon entry into force, will prevail over the domestic laws of Nepal.

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 Minister of Law and Justice of Nepal (or such other legal representative of the Government acceptable to MCC), in form and substance satisfactory to MCC;

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

(c) MCC will not have determined, at the time of this Compact's entry into force, that the Government has engaged in a pattern of actions inconsistent with the eligibility criteria for MCC Funding; and

(d) The conditions set forth in Annex V have been satisfied.

Section 7.3 Date of Entry into Force. This Compact will enter into force on the date of the letter from MCC to the Government in an exchange of letters confirming that MCC and the Government have completed their 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 to MCC's satisfaction.

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

Section 7.5 Provisional Application. Upon signature of this Compact, and until this Compact has entered into force in accordance with Section 7.3, the Parties will provisionally apply the terms of this Compact; provided that, no MCC Funding, other than Compact CDF, will be made available or disbursed before this Compact enters into force.

ARTICLE 8.

ADDITIONAL GOVERNMENT COVENANTS

Section 8.1 Covenant for the Electricity Transmission Project. The Government will ensure the full and expeditious cooperation of all relevant Government entities to ensure that all land acquisition, site access, and forest clearance required to implement the Compact is provided in a timely manner, and consistent with all MCC policies.

SIGNATURE PAGE FOLLOWS ON THE NEXT PAGE

IN WITNESS WHEREOF, each Party, by its duly authorized representative, has signed this Compact.

Done at Washington, DC, this 14th day of September, 2017, in the English language.

FOR THE UNITED STATES OF
AMERICA, acting through the
MILLENNIUM CHALLENGE
CORPORATION

FOR THE FEDERAL DEMOCRATIC
REPUBLIC OF NEPAL, acting
through the MINISTRY OF FINANCE

/s/

/s/

Name: Jonathan G. Nash
Title: Chief Executive Officer (Acting)

Name: Gyanendra Bahadur Karki
Title: Minister of Finance

**SIGNATURE PAGE TO MILLENNIUM CHALLENGE COMPACT
BETWEEN THE UNITED STATES OF AMERICA
ACTING THROUGH THE MILLENNIUM CHALLENGE CORPORATION
AND THE FEDERAL DEMOCRATIC REPUBLIC OF NEPAL
ACTING THROUGH THE MINISTRY OF FINANCE**

ANNEX I

PROGRAM DESCRIPTION

This Annex I describes the Program that MCC Funding will support in Nepal during the Compact Term.

A. PROGRAM OVERVIEW

1. Background and Consultative Process.

(a) Background.

Nepal was initially selected by MCC's Board of Directors to develop a threshold program in December 2011 based on the strength of its performance on MCC's policy indicators following a period of civil and political unrest in Nepal from 1996-2006. Before a threshold program was finalized, MCC's Board of Directors selected Nepal in December 2014 to develop a compact. In this selection decision, MCC's Board of Directors recognized Nepal's efforts to establish rule of law and democratic institutions and highlighted the importance to the United States and South Asia of a politically stable and economically-growing Nepal. Much of the work prepared for the threshold program, such as the constraints analysis, and certain power and transport policy and institutional analyses, were completed shortly after Nepal was selected to develop a compact and were repurposed for development of the compact.

Since December 2014, MCC and the Government have focused on developing a compact to address the identified constraints to growth in Nepal. Following consultations with the private sector, civil society, and development partners, the Government and MCC ultimately agreed to focus on two of the identified constraints: inadequate supply of electricity and the high cost of transport. Investment in Nepal's electricity sector is particularly critical due to the impacts of inadequate supply, as Nepal has historically suffered from the worst electricity shortages in South Asia. Demand for electricity has historically exceeded domestic electricity supply, resulting in load-shedding particularly during the dry winter months when hydropower generation is low. The under-supply of electricity is further exacerbated by high losses in transmission and distribution. Low availability of electricity creates significant costs for businesses, which have to run generators on expensive imported fuel.

With regard to the high cost of transport, this constraint has significant economic impacts due to the land-locked and mountainous nature of Nepal, as well as its reliance on cross-border trade. The Program will focus on road maintenance, which suffers from insufficient funding and ineffective technical and management practices.

(b) Consultative Process.

Since being selected to develop a compact, the Government's efforts in Nepal have focused on development of a compact designed around the identified constraints. Throughout the compact development process, the Government has engaged civil society, trade associations, development

partners, political parties, and other relevant communities and stakeholders to seek their support, guidance, and feedback in project design and risk mitigation.

To ensure the investments proposed for the Nepal Compact have the widest political support and the greatest potential for impact, MCC has worked closely with the United States Agency for International Development (“*USAID*”) and the United States Department of State, as well as the Government of India and a variety of development partners, to identify and design the investments described further in this [Annex I](#).

2. Description of Program and Beneficiaries.

(a) Program Description.

The Program focuses on two key binding constraints to economic growth – the inadequate supply of electricity and the high cost of transport. The root causes of Nepal’s power sector problems have contributed to low and slow investments in the electricity value chain, leading to a shortage of electricity caused by: slow expansion of domestic generation; low levels of electricity imports due to inadequate domestic and cross-border transmission infrastructure; and high technical losses in the system. The Program intends to alleviate the inadequate supply of electricity by increasing the flow of electricity from existing and future generation plants into the network, while also facilitating electricity trade with India. In combination, these elements are expected to reduce load-shedding and make new sources of domestic generation become financially viable. In addition, proposed technical assistance is intended to strengthen the planning and regulatory environment, thereby promoting enhanced private sector investment in the longer term.

With regard to the high cost of transport, which has significant economic effects due to the land-locked and mountainous nature of Nepal and its reliance on cross-border trade, the root cause analysis identified the potential causes as insufficient funding for the creation and maintenance of roads, inefficient customs and border enforcement, an inefficient trucking industry, and inadequate road coverage. The Program will focus on addressing insufficient funding for road maintenance by improving technical and management practices. Funding for road maintenance as well as technical assistance will be provided to the Department of Roads (the “*DOR*”) and to the Roads Board Nepal (the “*RBN*”) – which is the agency responsible for collecting and allocating road maintenance funds – to assist with the prioritization of investments.

(b) Beneficiaries.

The Program is expected to benefit more than five million households (approximately 23 million people) by the end of the Compact Term, as detailed below:

Project	ERR, Central Estimate	Beneficiaries ('000s) ¹		Beneficiary Population ²		
		Households	Individuals	<US\$2/day	US\$2-US\$4/day	>US\$4/day
Electricity Transmission Project	12%	5,035	22,659	7%	31%	62%
Road Maintenance Project	29%	205	925	8%	39%	53%

The beneficiaries of the Electricity Transmission Project are the population of grid-connected households within Nepal who are expected to experience increased availability of electricity for consumption as a result of the Project. The beneficiaries of the Road Maintenance Project are households living in village development committees and municipalities crossed by roads selected for periodic maintenance using MCC Funding.

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 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. Electricity Transmission Project

(a) Summary of Project and Activities.

The objective of the Electricity Transmission Project (the “*Electricity Transmission Project*”) is to increase domestic electricity supply for consumption by improving the availability and reliability of electricity in Nepal’s electricity grid. To achieve the Electricity Transmission Project Objective, MCC Funding will support the following expenditures as further detailed in this section: (i) construction of transmission lines to expand the high voltage transmission backbone inside Nepal and the Nepal side of a second cross-border transmission line with India; (ii) construction of three substations along the MCC-funded transmission lines; (iii) technical assistance activities to improve sustainability of the power sector and MCC investments; and (iv) necessary expenditures for project management, environmental and social impact assessment, and engineering and technical supervision to ensure the Electricity Transmission Project complies with MCC and Government of Nepal policies and standards.

¹ There is overlap between the beneficiaries of the Electricity Transmission Project and the Road Maintenance Project, hence total compact beneficiaries cannot be estimated by adding together the beneficiaries of each Project.

² Income categories based on constant 2005 PPP dollars.

(i) Transmission Lines Activity.

Through the Transmission Lines Activity, MCC Funding will be used to construct approximately 300 kilometers of a double-circuit 400 kilovolt transmission line inside Nepal that includes the following components: 1) a segment starting from the northeast of Kathmandu at Lapsipedi to the west of Kathmandu near Ratmate; 2) a segment from Ratmate to the industrial town of Hetauda, which is located south of Kathmandu; 3) another segment from Ratmate to Damauli to the west; 4) a segment from Damauli heading southwest toward Butwal; and 5) a link from Butwal to the Indian border.

(A) BIKAS Sub-Activity. In addition to construction of the transmission lines, the Transmission Lines Activity includes the “Benefit Integration through Knowledge-Sharing and Social Acceptance” sub-Activity or “**BIKAS.**” The goal of this sub-Activity is to build relationships within affected communities by delivering direct benefits that complement the improvements in electricity supply that will be realized by Nepal as a whole. Historically, transmission lines have crossed communities while contributing little to no direct benefits to their well-being. As a result of not realizing direct benefits and dissatisfaction with land valuation, communities in Nepal have often protested the construction of such infrastructure leading to disruptions, delays, and even damage to infrastructure assets. Recognizing potential challenges like these, the BIKAS sub-Activity seeks to pre-emptively provide services to communities beyond resettlement compensation and the environmental management measures typically found under environmental and social management plans. This approach both ensures that Project-affected communities experience clear gains from the Electricity Transmission Project and responds to lessons learned from other donor-funded projects in Nepal that suggest that this form of community engagement can help reduce opposition to and disruption of implementation of the Electricity Transmission Project. The final scope of this sub-Activity will be determined through a consultative process after Compact-signing, and may include a variety of services to ensure the affected communities are benefiting from the Program with an emphasis on electricity consumption. Possible benefit sharing services may include but shall not be limited to, connecting communities to the electricity grid as well as off-grid solutions using technology such as micro-hydro turbines or solar photovoltaic panels.

(ii) Substations Activity.

This Activity is complementary to the Transmission Lines Activity. MCC Funding will be used to construct three substations to increase or decrease transmitted voltages for further transmission or distribution to consumers. The substations will be located at or close to Ratmate, Damauli, and Butwal. Separately from the Program, the Government has agreed to upgrade two other substations that are connected to electricity pooling hubs along the transmission lines constructed as part of the Transmission Lines Activity, at or near Lapsephedi and Hetauda. The Government’s upgrade of substations at Lapsephedi and Hetauda will not be considered part of the Government’s contribution to the Program.

(iii) Power Sector Technical Assistance Activity.

This Activity aims to support the establishment of an independent electricity sector regulator (the Electricity Regulatory Commission or “**ERC**”), as well as capacity-building through technical

assistance to help bring transparency, efficiency, and competition into Nepal's power sector. MCC Funding will be used to embed experts within ERC to improve ERC's skills in rule-making, dispute resolution, and economic and technical regulation. Similarly, one or more advisors will be embedded in the Ministry of Energy, and/or the Department of Electricity Development to facilitate coordination of sector regulation. This Activity will also focus on helping the Nepal Electricity Authority ("NEA") improve its transmission business in the areas of regulatory cost recovery, improved grid operations, and better system planning. Specific efforts may involve: (a) training in system and market operations; (b) financial management system improvements for transmission transactions and assets; and (c) targeted human resource policies and job classifications, so that when the Government is ready to establish an independent transmission company, the NEA has the tools and skills to become an effective operation. This Activity will also support a study to examine and address key social issues such as low income and/or marginalized groups' ability to pay for electricity or access electricity and the institutionalization of a lifeline tariff into the Government's policy statement. Finally, the Activity will support NEA's Environment and Social Studies Department in strengthening institutional capacity in social impact assessment and inclusive stakeholder engagement through the development of guidelines, tools, and training.

(iv) Program Management and Technical Oversight Activity.

The Program Management and Technical Oversight Activity will complement the Transmission Lines and Substations Activities. To successfully implement the proposed Electricity Transmission Project infrastructure investments while complying with MCC's technical, environmental and social standards, MCC Funding will support necessary expenditures for Project management, environmental and social impact assessment and mitigation, and engineering and technical supervision of the Electricity Transmission Project.

(b) Beneficiaries.

The Electricity Transmission Project will affect all grid-connected consumers in Nepal. The Project will therefore benefit at least the 72 percent of households that are currently believed to be connected to the electricity grid. Given that Nepal's projected population at the end of the Compact is 31.5 million people, an estimated 23 million beneficiary individuals living in five million beneficiary households are expected to benefit from the Electricity Transmission Project.

(c) Environmental and Social Mitigation Measures.

The Electricity Transmission Project is classified as Category A in accordance with MCC's Environmental Guidelines. Based on a preliminary evaluation, seven of the eight International Finance Corporation Environment and Social Performance Standards (the "**IFC Performance Standards**"), which are incorporated by reference into the MCC Environmental Guidelines, will apply.

There are some unavoidable environmental and social impacts of the Electricity Transmission Project, such as tree cutting, land acquisition, and resettlement. However, consistent with MCC policies, all risks will be properly addressed through relevant compensation, mitigation, or management measures. Environmental and social considerations have already been taken into

account during route selection for the Transmission Lines Activity to avoid or minimize impacts to sensitive environmental and social characteristics of the Project areas. The Electricity Transmission Project will also complete a domestic environmental impact assessment permitting process and a subsequent forest clearance permitting process prior to the start of construction works. The BIKAS sub-Activity will also be implemented in those communities traversed by the Electricity Transmission Project that are not realizing direct benefits from construction of the Transmission Lines Activity. Environmental and social risks, impacts, and opportunities will be managed through an environmental and social management system for all Compact activities. MCC Funding will be used to undertake an environmental and social impact assessment, environmental and social management plan, and any necessary resettlement action plans.

(d) Social Inclusion and Gender Integration.

The Electricity Transmission Project, through the BIKAS sub-Activity, is intended to have significant and positive social benefits. The principal idea of benefit-sharing is to share the benefits resulting from infrastructure projects in order to satisfy the electricity needs of the concerned communities. The BIKAS sub-Activity intends to explore the provision of electricity and associated services to gain acceptance of the affected communities, keeping in mind the demographic and social context of those communities. Section B.1.a.iii of this [Annex I](#) further outlines proposed activities to better address social inclusion and gender integration issues related to the power sector.

(e) Donor Coordination.

Throughout the multi-year development of the Compact, MCC and the Government have engaged in an inclusive process that included consultations with the United States Government, Nepali communities and key private sector actors, non-government actors, and other donors as well as multilateral organizations. In particular, MCC worked closely with the World Bank and the Asian Development Bank in reviewing and agreeing on various power sector reforms required in Nepal for future programming by the two banks. MCC also consulted frequently with the United Kingdom's Department for International Development ("*DFID*") during its preparation of a political economy analysis of power sector reform.

(f) USAID.

The Electricity Transmission Project benefits from close inter-agency collaboration between MCC and USAID. Specifically, MCC has coordinated closely with USAID on its US\$10 million ongoing technical assistance activity, which provides a review of the Government's regulatory regime and provides ongoing assistance to the Government to achieve financial close on several large hydropower project transactions. USAID's assistance is complementary to MCC's efforts in the electricity sector.

(g) Sustainability.

Sustainability of the Electricity Transmission Project will be enhanced by investments in technical assistance that are focused directly on improving the regulatory regime to create greater transparency, accountability, and efficiency of the electricity market. Furthermore, the technical assistance provided under the Compact is intended to improve the Government's capacity to

better manage and maintain transmission assets. A sustained increase in the consumption of reliable and affordable electricity supply should promote economic growth, create jobs, increase incomes, and consequently reduce poverty.

(h) Policy, Legal, and Regulatory Reforms.

In addition to Section 8.1 of the Compact, the Parties have identified the following policy, legal, regulatory, and institutional reforms and actions that the Government will pursue in support of the Project. MCC and the Government agree that two key requirements for improvement of the electricity sector are (i) the creation of an independent electricity sector regulator, and (ii) passage of a new law for electricity sector regulation, which will grant the regulator the authority to license sector operators, provide operating certificates, set rates in the public interest, and make rules for transparent sector operations. Technical assistance for the proposed regulator and for the Ministry of Energy will be dependent upon passage of legislation creating the regulator and providing the regulator with the appropriate authorities

2. Road Maintenance Project

(a) Summary of Project and Activities.

The objective of the Road Maintenance Project (the “*Road Maintenance Project*”) is to maintain road quality across Nepal’s primary or strategic road network (the “*SRN*”). To achieve the Road Maintenance Project Objective, MCC Funding will support: (i) funding for technical assistance and capacity building to Nepal’s DOR and RBN, and (ii) up to 305 kilometers of maintenance works on Nepal’s SRN.

(i) Technical Assistance Activity.

This Activity will provide training and capacity building for the DOR and RBN. Compact funding will support training and capacity building for DOR and RBN, as applicable, in the areas of: 1) improved data collection and techniques; 2) preparation of appropriate road maintenance plans driven by economic justification; 3) improved prioritization of periodic maintenance; 4) improved contracting and contracting management, including integration of improved road safety features; and 5) improved project management. The training and capacity-building provided will also entail the transfer of modern road maintenance methods, technologies, and business processes under this Activity.

(ii) Strategic Road Maintenance Works Activity.

The Strategic Road Maintenance Works Activity is intended to complement and build upon the Technical Assistance Activity and will include two components: (i) a pilot sub-Activity focused on pavement recycling (the “*Pavement Recycling sub-Activity*”); and (ii) a matching fund to finance periodic maintenance works. The Pavement Recycling sub-Activity will be undertaken using new technology which has the potential to address some of the issues associated with carrying out works on narrow roads, namely traffic congestion, difficult work conditions, and extended construction times. This sub-Activity is proposed to be tested and evaluated prior to entry into force of the Compact to inform the remaining program design for the Strategic Road Maintenance Works Activity.

To incentivize additional Government spending on road maintenance, MCC Funding will be used to establish a matching fund that would provide US\$2 for every US\$1 the Government spends above its current average annual amount for periodic road maintenance up to a total of US\$15,000,000 annually for three years. The matching fund would be used to fund periodic road maintenance works on up to 305 kilometers in total, selected from a pool of 2,000 kilometers of Nepal's SRN. Using the HDM-4 Model, the Government has initially selected five road segments for periodic maintenance. At the time of implementation, if it is no longer feasible to perform periodic maintenance on the selected road segments, the Government will use the HDM-4 model to select substitute road segments of up to 305 kilometers in total. The overall program of works will be confirmed through a multi-year maintenance plan to be generated through technical assistance support of the Project, which will focus on utilization of improved data and an economic prioritization of works.

(b) Beneficiaries.

The Road Maintenance Project is estimated to benefit approximately 924,000 individuals (in approximately 205,000 households) spread over the local administrative units crossed by the proposed five road segments.

(c) Environmental and Social Mitigation Measures.

The Road Maintenance Project is classified as Category B under MCC's Environmental Guidelines where the proposed activities have potentially limited adverse environmental or social risks, or impacts that are few in number, generally site-specific, largely reversible, and readily addressed through mitigation measures. The Project is limited to maintenance and rehabilitation of existing roads and is unlikely to have significant adverse environmental and social impacts for which standard management measures are unavailable. Environmental or social impact caused by construction activities, such as temporary road closures, excavation and borrow pits, noise, dust, and worker and community health and safety, will be managed through targeted environmental and social management plans based on the findings of an abbreviated environmental and social impact assessment. No land acquisition or physical resettlement is anticipated.

In addition, the Road Maintenance Project will promote road safety through improved road design, and through information and awareness campaigns by the Government to help with more responsible and safer use of roads by both vehicle operators as well as non-motorized users of Nepal's primary or "strategic road network." The information and awareness campaign will raise awareness about truck and bus driver responsibilities, vehicle maintenance, and safe and responsible use of highways by both vehicles and pedestrians. To mitigate the accident risks, the Project will support building "shoulders" along selected roads with high incidents of accidents to pedestrians and non-motorized means of transport.

(d) Social and Gender Inclusion.

MCC Funding under the Road Maintenance Project will also be used to engage with contractors and the DOR to encourage the participation of women and marginalized groups in higher skilled and higher paying maintenance jobs.

(e) Donor Coordination.

There are two primary donors working on maintenance related work on the SRN: the Asian Development Bank and DFID. MCC will coordinate its technical assistance efforts under the Compact, to the extent possible, to reinforce these technical assistance efforts.

(f) USAID.

USAID is not currently funding any programs in Nepal specifically targeting the transport sector. Throughout the implementation of the Compact, MCC will coordinate with USAID if any transport-related activities are supported by USAID.

(g) Sustainability.

Investments in road maintenance are an investment in longer-term sustainability. The Road Maintenance Project is expected to help the Government move towards addressing its long-term maintenance needs through improved data collection on the SRN, improved maintenance planning, and prioritization, the mobilization of an appropriate amount of financial resources, and developing an improved system contractor performance mechanism.

(h) Policy, Legal, and Regulatory Reforms.

Road maintenance has suffered from inadequate resources and management practices not consistent with international best practices. Even though the RBN has been established to manage funding for maintenance, rehabilitation, reconstruction, pavement upgrading, and road safety, only part of the financial resources meant for road maintenance actually reach the RBN. To address these issues, development partners are providing technical assistance to the Government, including the RBN and DOR and assisting with the amendment or, if necessary, the replacement of the Road Board Act.

Both the technical assistance and the infrastructure components of the Road Maintenance Project should help raise DOR's capacity to manage road maintenance to international standards and use lessons learned to implement 305 kilometers of road maintenance projects, including the possible use of performance-based maintenance contracting. In particular, the matching fund should incentivize the Government to increase its road maintenance budget beyond the historic average.

C. IMPLEMENTATION FRAMEWORK

1. MCA-Nepal

(a) Structure and Establishment.

The Government will establish MCA-Nepal as a development board through passage of a formation order approved by the Council of Ministers and published in the Nepal Gazette. Development boards are independent and flexible entities, and are commonly used in Nepal to implement a variety of projects including foreign grant or loan-funded projects. MCA-Nepal will have full decision-making autonomy, including, *inter alia*, the ability, without the consent or

approval of any other party, to: (i) enter into contracts in its own name, (ii) sue and be sued, (iii) establish an account in a financial institution in the name of MCA-Nepal and hold MCC Funding in that account, (iv) expend MCC Funding, (v) engage contractors, consultants and/or grantees, including, without limitation, procurement and fiscal agents, and (vi) competitively engage one or more auditors to conduct audits of its accounts. The governance of MCA-Nepal will be set forth in more detail in the Program Implementation Agreement, the formation order and internal regulations of MCA-Nepal (“**Internal Regulations**”) or as otherwise agreed in writing by the Parties. The Internal Regulations will be in accordance with the Governance Guidelines.

MCA-Nepal will be administered, managed and supported by the following bodies: a board of directors (the “**Board of Directors**”), a management unit (the “**Management Unit**”), and one or more Stakeholders Committees. MCA-Nepal will use various Government entities to help implement the Projects.

(b) Board of Directors.

The Board of Directors will have ultimate responsibility for the oversight, direction, and decisions of MCA-Nepal, as well as the overall implementation of the Compact. The Board of Directors will be comprised of seven voting members. As of the date hereof, the voting members of the Board of Directors will include the following representatives:

- (i) the Finance Secretary of the Ministry of Finance;
- (ii) a Joint Secretary of the Ministry of Energy;
- (iii) a Joint Secretary of the Ministry of Physical Infrastructure and Transport;
- (iv) the Executive Director of MCA-Nepal;
- (v) the Managing Director of the Nepal Electricity Authority;
- (vi) a representative from civil society; and
- (vii) a private sector representative.

The number of voting members and their identities may be changed through amendments to the Internal Regulations with MCC’s approval. The members of the Board of Directors may be represented by alternates appointed pursuant to MCA-Nepal’s Internal Regulations. In addition, MCC’s Resident Country Director in Nepal will serve as a non-voting observer to the Board. In addition, representatives from the following ministries, as well as any other experts the Board of Directors finds helpful, may be invited on an as needed basis: (a) the Ministry of Land Reform and Management, (b) the Ministry of Home Affairs, (c) the Ministry of Forests and Soil Conservation, and (d) the Ministry of Population and Environment.

The process of selecting the Board members will be further stipulated in the Internal Regulations and will be consistent with the Governance Guidelines.

(c) Management Unit.

The Management Unit, 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.

The Management Unit will be led by an Executive Director and will be composed of the directors and officers as agreed between the Parties and consistent with the Governance Guidelines. The Management Unit will be selected after an open, competitive, and non-discriminatory recruitment and selection process (or its equivalent), and the appointment of each member of the Management Unit is subject to MCC no-objection. The officers will be supported by appropriate additional staff to enable the Management Unit to execute its roles and responsibilities. Upon written notice by MCC to MCA-Nepal, the selection of candidates for additional positions within MCA-Nepal will be subject to MCC approval.

(d) Stakeholders' Committees.

The Parties recognize the importance of establishing one or more stakeholders' committees, (each, a "***Stakeholders' Committee***"), both to promote transparency and ongoing consultation among Compact stakeholders, as well as to further the overall goals and objectives of the Compact. The Stakeholders' Committee will be identified and operated in accordance with procedures described in the Governance Guidelines and the Stakeholder Engagement Plan (the "***SEP***"). The Parties agree that (a) MCA-Nepal will regularly update the SEP; (b) MCA-Nepal will ensure that each Stakeholders' Committee identified in the SEP will meet or engage in coordinated collaboration with MCA-Nepal on at least a semi-annual basis; (c) the SEP will provide MCA-Nepal's oversight and procedures for receiving, sharing, and responding to feedback from and in collaboration with each Stakeholders' Committee identified in the SEP; and (d) MCA-Nepal will provide regular updates regarding the SEP to its Board of Directors.

2. Project Partners.

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 assist with implementation and carry out any Project or Activity (or a component thereof) under this Compact (each, a "***Project Partner***"). The appointment of any Project Partner will be subject to review and approval by MCC. The Government will ensure that the roles and responsibilities of each Project Partner and other appropriate terms are set forth in an agreement, in form and substance satisfactory to MCC (each a "***Project Cooperation Agreement***").

3. Fiscal Agent.

Unless MCC agrees otherwise in writing, the Government will engage a fiscal agent (a "***Fiscal Agent***"), which will be responsible for assisting the Government with its fiscal management and assuring appropriate fiscal accountability of MCC Funding, and whose duties will include those set forth in the Program Implementation Agreement and such agreement as the Government enters into with the Fiscal Agent, which agreement will be in form and substance satisfactory to MCC.

4. Procurement Agent.

Unless MCC agrees otherwise in writing, the Government will engage one or more procurement agents (collectively, the “*Procurement Agent*”) to carry out and certify specified procurement activities in furtherance of this Compact. The roles and responsibilities of the Procurement Agent will be set forth in the Program Implementation Agreement or such agreement as the Government enters into with the Procurement Agent, which agreement will be in form and substance satisfactory to MCC. The Procurement Agent will adhere 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.

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 Contribution.

The Government Contribution may include in-kind and financial contributions (including obligations of Nepal 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 complement MCC Funding through budget allocations to the Compact Program. The Government Contribution is US\$130,000,000. The Government Contribution includes a contribution of US\$40,000,000 following Compact-signing but prior to entry into force of the Compact. The remaining contribution of US\$90,000,000 will be committed by the Government prior to the initial disbursement of Program Funding and subsequently disbursed within the Compact Term. The Government Contribution is exclusive of the Government’s other obligations in the Compact including exemption of all Taxes. The Government Contribution will be subject to any legal requirements in Nepal 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 this Government Contribution, which requirements may be conditions precedent to the Disbursement of MCC Funding.

EXHIBIT A TO ANNEX II
MULTI-YEAR FINANCIAL PLAN SUMMARY

(US\$)								
Component	CDF	Year 1	Year 2	Year 3	Year 4	Year 5	Total	
1. Electricity Transmission Project								
(a) Transmission Lines Activity	2,489,000	55,677,000	41,235,000	41,235,000	55,320,000	32,291,000	228,247,000	
(b) Substations Activity	2,050,000	19,712,000	22,122,000	22,122,000	30,121,000	17,895,000	114,022,000	
(c) Power Sector Technical Assistance Activity	435,000	6,398,000	4,054,000	2,886,000	4,331,000	4,301,000	22,405,000	
(d) Program Management and Technical Oversight Activity	17,375,000	4,115,000	3,207,000	3,207,000	4,207,000	1,448,000	33,559,000	
Subtotal	22,349,000	85,902,000	70,618,000	69,450,000	93,979,000	55,935,000	398,233,000	
2. Road Maintenance Project								
(a) Technical Assistance Activity	2,632,000	1,843,000	1,227,000	1,142,000	165,000	36,000	7,045,000	
(b) Strategic Road Maintenance Works Activity	3,520,000	1,033,000	11,645,000	16,011,000	13,031,000	---	45,240,000	
Subtotal	6,152,000	2,876,000	12,872,000	17,153,000	13,196,000	36,000	52,285,000	
3. Monitoring and Evaluation								
M&E Component Activities	198,000	732,000	1,977,000	1,898,000	1,355,000	3,332,000	9,492,000	
4. Program Management and Administration								
(a) MCA-Nepal Program Administration	9,281,000	2,480,000	2,550,000	2,020,000	2,553,000	4,466,000	23,350,000	
(b) Procurement, Fiscal, and Audit Services	2,520,000	4,110,000	2,310,000	2,310,000	2,310,000	3,080,000	16,640,000	
Subtotal	11,801,000	6,590,000	4,860,000	4,330,000	4,863,000	7,546,000	39,990,000	
MCC INVESTMENT	40,500,000	96,100,000	90,327,000	92,831,000	113,393,000	66,849,000	500,000,000	
GOVERNMENT CONTRIBUTION	40,000,000	----- 90,000,000 -----						130,000,000
GRAND TOTAL	80,500,000						630,000,000	

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-Nepal will: (i) monitor to determine whether the Projects are on track to achieve their intended results (“*Monitoring Component*”); and (ii) 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 the Program. The M&E Plan will also include any monitoring and evaluation (“*M&E*”) requirements that MCA-Nepal must meet in order to receive Disbursements, and will serve as a communication tool so that MCA-Nepal staff and other stakeholders clearly understand the objectives and targets the MCA-Nepal 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-Nepal and on the MCC Website.

2. Program Logic

The M&E Plan will summarize the clearly defined Project-level logic models, which for each Project will illustrate how the Activities, and sub-Activities (as necessary) contribute to the Project Objectives and Compact Goal. All logic models will clearly summarize the outputs, outcomes, and goal expected to result from the Program. A description of the logic underlying each Project is included below:

(a) Electricity Transmission Project

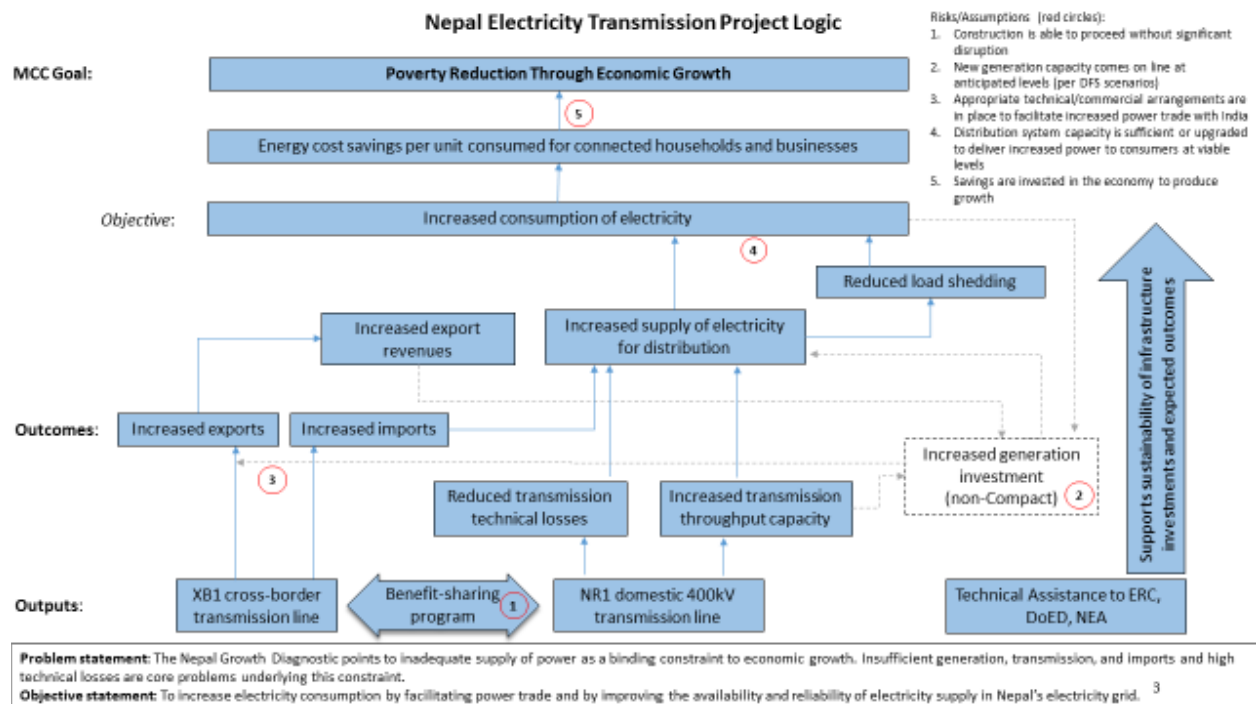
The objective of the Electricity Transmission Project is to increase electricity consumption by improving the availability and reliability of electricity supply in Nepal’s electricity grid and by facilitating power trade. Compact investments in Nepal’s transmission network and cross-border interconnection will support increased supply of electricity to consumers by providing a path for delivery for a pipeline of new domestic electricity generation as well as increased electricity trade with India. The transmission backbone will allow more efficient movement of electricity across the grid, with lower technical losses, such that supply is better able to meet demand. This is contingent on the pipeline of domestic generation coming to fruition in a timely manner or the successful introduction of increased cross-border electricity trade with India.

The cross-border interconnection will facilitate the import of electricity from India to meet demand, particularly in the dry season when domestic generation is at its lowest. It will also facilitate exports to India in the rainy season when domestic generation is expected to exceed domestic demand. Export revenues are expected to facilitate more investment in domestic generation by the Government and private investors including independent power producers and electricity traders. Results related to electricity trade with India are contingent on the negotiation of power trade agreements between Nepal and India and the appropriate calibration of the two grids, both of which are directly addressed by the Government.

The Power Sector Technical Assistance Activity investments in establishing a new regulator and assisting the Government with better planning, cost recovery, and grid operation will result in: 1) a power sector that balances the economic and financial interests for sector stakeholders and promotes the safe operation of the grid; and 2) improved sustainability of MCC infrastructure investment by enabling NEA to operate, manage, and maintain the new 400 kilovolt (“kV”) system, with which it has no prior experience. These investments are expected to increase the financial and physical sustainability of the infrastructure investment.

The increase of electricity in Nepal’s grid is expected to increase the amount of electricity supplied to consumers and increase electricity trade with India. Increased, more reliable, and potentially more affordable electricity should allow consumers to use more electricity to meet their energy needs and incur less expenditures per unit of energy consumed than experienced currently. The savings generated from this are expected to be reinvested to produce growth and reduce poverty.

A detailed program logic diagram for the Electricity Transmission Project is below.



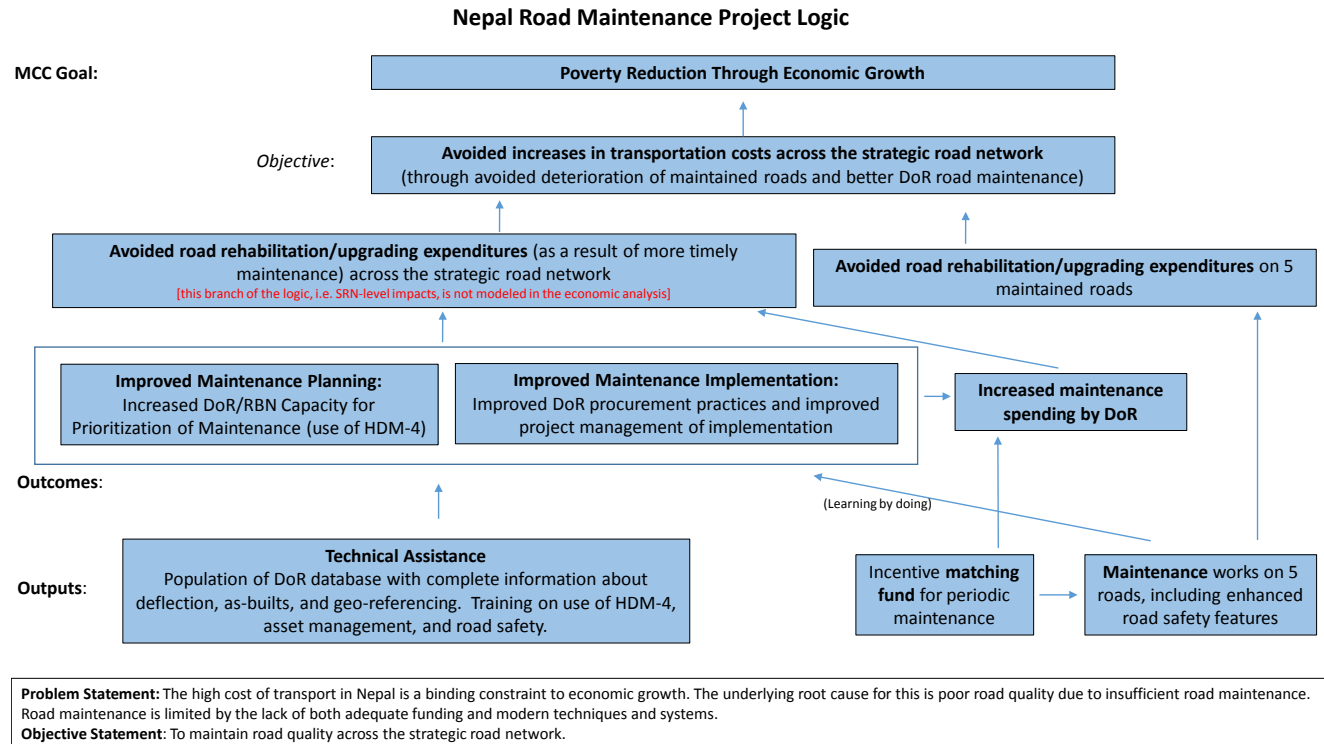
The M&E Plan will also outline key assumptions and risks that underlie the accomplishment of the theory of change summarized in the program logic. However, such assumptions and risks will not excuse any party's performance unless otherwise expressly agreed to in writing by the other party. The known assumptions and risks for the Electricity Transmission Project include:

- (i) Implementation delays;
- (ii) Appropriate technical/commercial arrangements and infrastructure are in place to facilitate increased electricity trade with India;
- (iii) Slow commissioning of domestic new generation projects can reduce utilization of the electricity transmission line;
- (iv) Slow implementation of complementary transmission and distribution projects can restrict delivery of electricity to consumers;
- (v) Land acquisition is too slow and difficult to execute;
- (vi) Communities oppose MCC projects;
- (vii) Failure to enact legislation to authorize the electricity regulator and to fund its initial and ongoing operations; and
- (viii) Savings from cheaper electricity are invested in the economy to produce growth.

(c) Road Maintenance Project

The objective of the Road Maintenance Project is to maintain road quality across the SRN. First, this Project will provide technical assistance related to road maintenance planning, assessment, and implementation to strengthen the DOR's and RBN's capacity to plan and execute routine and periodic maintenance. Second, these interventions will be reinforced through a learning-by-doing approach to conducting maintenance on a subset of the SRN. This maintenance work will reduce road roughness and associated vehicle operating costs. These funds will be applied using a matching scheme aimed at incentivizing allocation of greater amounts of road maintenance resources. The expectation is that by equipping the DOR with the data, skills, and experience necessary to plan and implement road maintenance, combined with an increased level of funding under an improved road maintenance funding regime, the SRN will be adequately maintained and the road quality will not deteriorate.

A detailed program logic diagram for the Road Maintenance Project is below.



The known assumptions and risks for the Road Maintenance Project include:

- (i) The Project does not receive strong political and institutional support making implementation uncertain and risky; and
- (ii) Construction capacity to perform high quality works in a timely manner is low.

3. Projected Economic Benefits and Beneficiaries

3.1 Economic Benefits

(a) Electricity Transmission Project

The primary benefit from the Electricity Transmission Project is an increase in the supply of electricity to Nepali consumers. A separate but related benefit results from a decrease in load-shedding so that electricity is available for a greater proportion of the day. Incremental improvements in the supply of electricity would be the result of increased imports from India, increases in domestic production, and decreases in technical losses from the newly constructed, higher capacity transmission system. Decreases in load-shedding are expected as a result of increased supply of electricity to the system and continued improvements at the distribution and sub-transmission level.

Exports are a separate benefit stream valued at the tariff rate for electricity sales to India, as benefits for Indian consumers are not counted in the economic rate of return (“*ERR*”) estimate. While this means that exports are technically valued at a lower rate than domestic consumption in the *ERR*, the opportunity cost of Nepal’s exports is lower as well, since much of this electricity would otherwise be spilled. Moreover, sales of wet season surplus electricity are critical for encouraging new investments from independent power producers.

In addition to *MCC* costs, the *ERR* model includes cost contributions from the Government, costs paid in user fees, and estimated costs of complementary investments in new generation attributable to the Project. Benefits, including electricity consumed, imports, exports, and reductions in transmission losses, are estimated for years 2023 and 2030. The economic analysis assumes that Nepal’s electricity generation capacity will increase by 360 percent between 2016 and 2023 (from 856 megawatts (“*MW*”) to 3,946 *MW*).

The estimated *ERR* for the Electricity Transmission Project is 12 percent.

(b) Road Maintenance Project

The Road Maintenance Project is designed to maintain road quality across the *SRN* by promoting improved road maintenance practices. The Project will provide technical assistance to the *DOR* and *RBN* and hands-on learning through the maintenance of approximately 305 kilometers of roads. Maintenance interventions will include pavement improvement (overlays or surface dressings), safety enhancements, and slope stability improvements to reduce road closures caused by landslides.

Roads that will receive periodic maintenance under the Project were selected through a prioritization process that analyzed the economic efficiency of maintenance interventions by road. The selection started with a schedule of approximately 2,000 kilometers of roads proposed by the *DOR*, all of which are part of the *SRN*. The economic returns to periodic maintenance of these 2,000 kilometers were estimated using the *HDM-4* Model, which estimates the increase in consumer surplus from a decline in transport costs as represented by the decrease in vehicle operating costs and travel time caused by a road improvement. Roads were then ranked by the ratio of economic benefit to cost and those with the highest benefit-to-cost ratio, within the available budget envelope, were selected for Compact-funded maintenance. This prioritization resulted in the selection of five roads in Nepal’s Eastern, Central, and Mid-Western development regions, comprising a total of approximately 305 kilometers.

The five roads selected for periodic maintenance currently have relatively high traffic volumes compared to many other roads in Nepal and the road surfaces are in poor condition (high international roughness index (“*IRI*”) values). However, the roads have not deteriorated to the point where a major rehabilitation is required. The purpose of the periodic maintenance interventions is to prevent further deterioration that would be very expensive to repair. The economic analysis assumes that traffic growth will be the same in the “with Project” and the “without Project” scenarios. In other words, only normal traffic growth is assumed in the *HDM-4* models; no assumption is made regarding the Project’s potential to generate additional traffic.

Comparing Project cost with the economic benefit of road maintenance over a 20-year period, as estimated by HDM-4, the present value of economic costs comes to US\$38,400,000, the present value of benefits is US\$158,500,000, and the net present value of the Project is US\$120,100,000.

The estimated ERR for the Road Maintenance Project is 29 percent.

3.2 Beneficiary Analysis

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 ERR analysis that seeks to disaggregate the total increase in income to determine specifically which segments of society will benefit from the Program. MCC considers beneficiaries³ to be those people who experience better standards of living as a result of the Program through higher real incomes. The expected beneficiaries the Program are shown in the following table:

Project	Estimated Beneficiaries
Electricity Transmission Project	23 million*
Road Maintenance Project	0.92 million*
*There is some overlap, hence the Project beneficiaries cannot be added together to estimate Compact beneficiaries.	

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 the Compact Term as necessary.

4.1 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.

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

(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 gender, income level, 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. These will be denoted by the Common Indicator code.

(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-Nepal 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-Nepal 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:

Electricity Transmission Project:					
Result	Indicator	Definition	Unit	Baseline	Compact Target
Outcome Indicators					
Reduced Load-Shedding	Load-shedding	The deliberate shutdown of electric feeders, generally to prevent the failure of the entire electricity system when power supply is lower than demand at transmission level. Calculated as the annual difference between supply delivered through the distribution system and estimated load.	Gigawatt hours (“ GWh ”)	3,161 (2016) Source: NEA 2014/15 Annual Report, p109 (Projected Consumption) NEA 2015/16 Annual Report, p 124 (Total Available Electricity, minus Losses)	1,726.4 (2023) Source: PSSE in TT Feasibility Study (Volume 1, Table 3.23)
Increased Imports	Imported electricity	Annual quantity of electricity purchased from India	GWh	1,758.41 (2016) Source:	5,823.2 (2023)

Electricity Transmission Project:

Result	Indicator	Definition	Unit	Baseline	Compact Target
				NEA 2015/6 Annual Report, page 120, 124	Source: PSSE in TT Feasibility Study (Volume 1, Table 3.23)
Increased Exports Increased Revenues from Exports	Exported electricity	Annual quantity of electricity sold to India	GWh	3.25 (2016) Source: NEA 2015/6 Annual Report, page 124	2,895.8 (2023) Source: PSSE in TT Feasibility Study (Volume 1, Table 3.23)
Reduced Transmission Technical Losses	Transmission system technical losses (%)	1- (Total megawatt hours transmitted out from transmission substations/Total megawatt hours received from generation to transmission substations)	Percentage	4.82% (2016) Source: NEA 2015/6 Annual Report, page 38 (2072/73 in Nepali years)	1.89% (2023) Source: PSSE in TT Feasibility Study (Volume 1, Table 3.23)
Increased utilization of Transmission Network	Capacity utilization factor of a transmission line	The ratio of peak loading on the transmission line (in amperes) segment in a quarter and design capacity of the line. (Disaggregation by transmission line segment)	Percentage	0%	TBD
Benefit Sharing Keeps Construction on Schedule	Days of work missed	Number of days reported by the construction contractor that work must be stopped due to community unrest	Number	TBD	TBD
Economic/ERC: Balancing the financial and economic interests of the sector stakeholders.	TBD	TBD	TBD	TBD	TBD
Technical/ERC: Promoting the safe and reliable operation of the system.	TBD	TBD	TBD	TBD	TBD

Electricity Transmission Project:

Result	Indicator	Definition	Unit	Baseline	Compact Target
Licensing/ERC: Establishing and Monitoring the Legal Framework for Efficient Power Sector Operations.	TBD	TBD	TBD	TBD	TBD
Stakeholder/ERC: Provide a mechanism for licensees, consumers, and other stakeholders to resolve disputes and to provide public consultations.	TBD	TBD	TBD	TBD	TBD
Assist NEA to implement its obligation to comply with transmissions regulations as defined by an independent regulator	TBD	TBD	TBD	TBD	TBD
Improving NEA's transmission system planning and project preparation activities	TBD	TBD	TBD	TBD	TBD
Improve NEA's capacity to manage and operate its transmission system	TBD	TBD	TBD	TBD	TBD
Improve DOED's performance in management and oversight of the electricity sector	TBD	TBD	TBD	TBD	TBD
Output Indicators					
Transmission Infrastructure	Transmission throughput capacity added	The increase in throughput capacity, measured in megawatts, added by new, reconstructed, rehabilitated, or upgraded transmission lines	Megawatts	0	3,920 Source: WSP Technical Directive 6,

Electricity Transmission Project:

Result	Indicator	Definition	Unit	Baseline	Compact Target
		that have been energized, tested, and commissioned with MCC support. <i>This is the throughput capacity for each of the five segments of transmission lines individually.</i> <i>New Hetauda – Ratmate 400 kV D/C</i> <i>Ratmate to Lapsiphedi 400 kV D/C</i> <i>Ratmate to New Damauli 400 kV D/C</i> <i>New Damauli to New Butwal 400 kV D/C</i> <i>New Butwal to Indian Border (Further to Gorakhpur, India)</i>			Mission Report, March 2017, Annex E, pg 2, Table 2
Substation Infrastructure	Transmission substation capacity added	The total added transmission substation capacity, measured in mega volt-amperes, which is energized, commissioned, and accompanied by a test report and supervising engineer’s certification resulting from new construction or refurbishment of existing substations that is due to MCC support. <i>In Nepal, this comprises 3 400/220 kV Substations in New Butwal, New Damauli, and Ratmate.</i>	Mega volt ampere	0	Total: 2,330 Ratmate (640) New Damauli (640) New Butwal (1,050) Source: WSP Technical Directive 6, Mission Report, March 2017, Annex E, pg 1
Transmission Infrastructure	Km transmission lines upgraded or built	The sum of linear km of new, reconstructed, rehabilitated, or upgraded transmission lines that have been energized, tested, and commissioned with MCC support. <i>In Nepal, this comprises a 400kV transmission line within the East-West transmission backbone and the Nepal side of the New Butwal border connection to India. The indicator target reflects that both the NR1 and XB1 projects include two circuits; therefore, the length of the line is doubled.</i>	Kilometers	0	NR1 – New Damauli to Ratmate: 88.23 km NR1 – Ratmate to Lapsiphedi: 57.83 km NR1 – Ratmate to New Hetauda: 55.59 km New Damauli to New Butwal: 84 km XB1/New Butwal to Indian Border: 23 km

Electricity Transmission Project:

Result	Indicator	Definition	Unit	Baseline	Compact Target
					Total: 617.3km Source: TT DFS Report, Vol. 9, p.4 (XB1 and N Butwal-N Damauli); p.116 (remaining three segments)
Substation Infrastructure	Length of entry road constructed	The length of entry road constructed to approach the substation.	Kilometers	0	3.3 Source: TT DFS Report, Vol. 9, p.125, Scenario 3
Benefit Sharing Activities Implemented	TBD	TBD (Connections or provision of more electricity)	TBD	TBD	TBD
Economic/ERC: Balancing the financial and economic interests of the sector stakeholders.	TBD	TBD	TBD	TBD	TBD
Technical/ ERC: Promoting the safe and reliable operation of the system.	TBD	TBD	TBD	TBD	TBD
Licensing/ERC: Establishing and Monitoring the Legal Framework for Efficient Power Sector Operations.	TBD	TBD	TBD	TBD	TBD
Stakeholder/ERC: Provide a mechanism for licensees, consumers, and other stakeholders to resolve disputes and to provide public consultations.	TBD	TBD	TBD	TBD	TBD
Assist NEA to implement its obligation to comply with transmissions	TBD	TBD	TBD	TBD	TBD

Electricity Transmission Project:

Result	Indicator	Definition	Unit	Baseline	Compact Target
regulations as defined by an independent regulator					
Improving NEA's transmission system planning and project preparation activities	TBD	TBD	TBD	TBD	TBD
Improve NEA's capacity to manage and operate its transmission system	TBD	TBD	TBD	TBD	TBD
Improve DOED's performance in management and oversight of the electricity sector	TBD	TBD	TBD	TBD	TBD

Road Maintenance Project

Result	Indicator	Definition	Unit	Baseline	Compact Target
Outcome Indicators					
Avoided increases in transportation costs across the SRN	Roughness performance of the SRN	The share of the SRN that falls into bad (IRI>8), poor (6<IRI<8), fair (4<IRI<6), and good (IRI<4) categories of road roughness, by Nepali standards. Road roughness will be measured in terms of the International Roughness Index.	Percentage	2015/16:	CED:
Avoided road rehabilitation/upgrading expenditures				Bad: 44%	Bad: 43%
				Poor: 34%	Poor: 33%
				Fair: 15%	Fair: 15%
				Good: 6%	Good: 9%
				Source: iMC Task 1 Report, Executive Summary	Source: calculation based on improvement of 305km from bad/poor to fair/good
	Surface distress performance of the SRN	The share of SRN that falls into poor (3.1<SDI<5), fair (1.8<SDI<3), and good (SDI<1.8) categories of road surface distress, by Nepali standards. Surface distress will be measured in terms of the surface distress index (" <i>SDI</i> ").	Percentage	2015/16:	CED:
				Poor: 18%	Poor: 18%
				Fair: 77%	Fair: 77%

Road Maintenance Project

Result	Indicator	Definition	Unit	Baseline	Compact Target
				Good: 4%	Good: 4%
				Source: iMC Task 1 Report, Executive Summary	Source: iMC Task 1 Report, Executive Summary
Improved maintenance implementation	DOR annual maintenance expenditures	Annual DOR spending on routine, recurrent, and periodic maintenance.	US\$	2014/15: 35.8M (3.692B Nepali Rupees converted at 103.16 NPR/US\$) Source: iMC Task 1 Report, p. 13	US\$22.5M above spending in the year prior to the start of the compact maintenance works, cumulative over 3 years Source: Road Maintenance Project design
Output Indicators					
Maintenance works	Kilometers of roads completed	The length of roads in km on which construction of new roads or reconstruction, rehabilitation, resurfacing or upgrading of existing roads is complete (certificates handed over and approved). <i>The targeted road segments initially include: H02: Hetauda – Bhimphedi, H07: Charali – Phidim, H08: Dharan – Basantapur/Chitre, H09: Kadmaha – Gaighat, and H11: Amelia – Tulsipur.</i>	Kilometers	0	Total: Up to 305 (the exact target will be updated based on signed maintenance contracts) Source: RMP design and 2017 RMP CBA
Maintenance works	Roughness	The measure of the roughness of the road surface, in meters of height per kilometer of distance traveled. This measure reflects the IRI at completion of Compact-funded road maintenance works. <i>Calculated as sum of IRI measure per kilometer / total road length.</i>	Meters per kilometer	H07 (Charali – Phidim): 8.0 H08 (Dharan – Basantapur/Chitre): 8.9 H09 (Kadmaha – Gaighat): 9.0	At contract completion (estimated 2022): H07: 3.5 H08: 3.5 H09: 3.5 H02: 4.1 H11: 3.5 Source: 2017 RMP CBA

Road Maintenance Project					
Result	Indicator	Definition	Unit	Baseline	Compact Target
				H02 (Hetauda – Bhimpheedi) : 9.8 H11 (Amelia-Tulsipur) 7.1 (2016) Source: 2017 RMP CBA	
Technical Assistance	Population of Highway Management Information System database	Date on which Highway Management Information System database is complete with updated as-built and deflection data for entire network.	Date	N/A	TBD
Matching Fund	DOR annual maintenance budget	Annual DOR budget allocated for routine, recurrent, and periodic maintenance.	US\$	FY 2016: 40M (4.28B Nepali Rupees converted at 103.16 NPR/US\$) Source: iMC Task 1 Report, page 9	US\$22.5M above spending in the year prior to the start of the compact maintenance works, cumulative over 3 years Source: RMP design

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.

Every Project must undergo a comprehensive, independent evaluation (impact and/or performance) in accordance with the MCC M&E Policy. 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 be acceptable to MCC and ensure non-biased results and the publication of results.

For each independent evaluation, MCA-Nepal 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.

(b) Electricity Transmission Project:

The evaluation of the Electricity Transmission Project is expected to be a performance evaluation based largely on quantitative data. It will make use of generation, load flow, and export/import data over time to assess what impacts may be the result of the MCC investment. It will likely include a household or business data collection component to assess the high level impacts, such as electricity consumption and expenditure per energy unit among grid customers. The evaluation will include a process study, assessing the fidelity of implementation to the original design, and setting the stage for the assessment of results further down the logical chain. The questions that will guide the design of the evaluation include:

- Was the Electricity Transmission Project implemented as planned? Did the quality of the work meet the specifications initially laid out?
- Was load-shedding in Nepal reduced as a result of the Electricity Transmission Project? This question links to the following outcome indicator: Load-shedding.
- How was cross-border electricity trade changed by the Electricity Transmission Project? This question links to the following outcome indicators: Imported Electricity and Exported Electricity.
- Did the Electricity Transmission Project increase the consumption of on-grid electricity by households and businesses in Nepal? This question links to the following outcome indicator: Electricity consumption per capita, which is the Project Objective.
- Did the BIKAS approach to transmission projects reduce community resistance to the Project, and construction delays? This question links to the following outcome indicator: Days of Work Missed.
- Additional evaluation questions related to the technical assistance provided through Activity 1.3 will be articulated later, once the targeted results are better understood.

The M&E Plan will contain the evaluation Indicators listed in the following table:

Electricity Transmission Project:							
Result	Indicator	Definition	Unit	Baseline	Target	Target Date	
Outcome Indicators							
<p>Cost Savings to Households and Businesses</p> <p>Project Objective: Increased Electricity Consumption</p> <p>Increased Supply for Distribution</p>	Electricity consumption per capita	The quantity of electricity consumed annually per capita in Nepal.	kWh/capita	<p>133 (2016)</p> <p>Source: NEA Annual Report 2015/6 (Total Sales of Electricity), Government of Nepal Central Bureau of Statistics, Population Projection 2011-2031, National Population and Housing Census 2011, Volume 8 NHPC 2011 (2016 Population Estimate)</p>	394	<p>Source: PSSE in TT Feasibility Study (Volume 1, Table 3.23, Consumption minus 15% Technical Losses), divided by a population estimate of 32,759,302.</p>	2023

(c) Road Maintenance Project:

The evaluation of the Road Maintenance Project is expected to be a performance evaluation with quantitative and qualitative components. One component will be economic modeling using the HDM-4 Model. This approach will require an independent assessment of road quality data across the SRN both before and after the MCC investments. The final independent assessment and HDM-4 model should occur at least 2-3 years after completion of the Project works. The independent evaluator will assess the HDM-4 calculations that went into the investment decision and determine whether baseline data collection is required to update the model. This quantitative component to the evaluation will speak to the effectiveness of both the technical assistance and maintenance works because it will evaluate achievement of the overall Project Objective of avoiding increases in transportation costs across the SRN. The qualitative component of the evaluation will attempt to capture the effectiveness of the technical assistance on improving DOR's maintenance planning and implementation. This may include process evaluation to map how processes have changed from baseline to endline and/or document review and observation. The questions that will guide the design of the evaluation include:

- What is the economic return – calculated in terms of vehicle operating cost savings and travel time savings – of the road maintenance investment? This question links to the following outcome indicators: road roughness and surface distress index.
- What are the relevant road authority’s current maintenance practices and what is the likelihood that MCC’s investment will remain adequately maintained? What were the effects of investments in improved maintenance? Has maintenance of the overall network improved? These questions link to the outcome indicator tracking road maintenance expenditures and the pending indicators related to improved maintenance planning and implementation.

Road Maintenance Project						
Result	Indicator	Definition	Unit	Baseline	Target	Target Date
Outcome Indicators						
Project Objective: Avoided increases in transportation costs across the SRN Avoided road rehabilitation/upgrading expenditures	Roughness	The measure of the roughness of the road surface, in meters of height per kilometer of distance traveled. <i>Calculated as sum of International Roughness Index (IRI) measure per kilometer / total road length.</i>	Meters per kilometer	H07: 8.0 H08: 8.9 H09: 9.0 H02: 9.8 H11: 7.1 (2016) Source: 2017 RMP CBA	H07: 3.7 H08: 3.8 H09: 3.7 H02: 4.4 H11: 3.7 Source: 2017 RMP CBA	3 years post completion of works

(d) Self-Evaluation.

Upon completion of the Compact Term, both MCC and MCA-Nepal will comprehensively assess three fundamental questions: (i) Did the Program meet the Project Objectives; (ii) Why did the Program meet or not meet the Project Objectives; and (iii) What lessons can be learned from the implementation experience (both procedural and substantive). The MCA-Nepal staff will draft the Compact Completion Report (“CCR”) in the last year of the Compact Term to evaluate these fundamental questions and other aspects of Program performance. Each MCA-Nepal department will be responsible for drafting its own section to the CCR for its own activities, subject to cross-departmental review. After MCA-Nepal staff drafts the CCR, relevant MCC staff will draft a Compact performance review. Similar to the CCR, each MCC division will be responsible for drafting its own section of the document, subject to cross-department review.

(e) 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 are to 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 in 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.

8. 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-Nepal with

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

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-Nepal leadership and sector leads, the MCC Resident Country Mission, and other MCC staff (such as Environmental and Social Performance and Gender and Social Inclusion), as well as external stakeholders, as applicable. While the entire M&E Plan must be developed collaboratively, MCC and MCA-Nepal 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.

9. 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 proposed by MCA-Nepal must be submitted to MCC for prior written approval. The M&E Plan may undergo peer review within MCC before the beginning of the formal approval process.

10. 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-Nepal will develop a post-Compact M&E Plan designed to observe the persistence of benefits created under this Compact. This plan should describe future monitoring and evaluation activities, identify the individuals and organizations that will 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.

ANNEX IV

CONDITIONS PRECEDENT TO DISBURSEMENT OF COMPACT CDF

This Annex IV sets forth the conditions precedent applicable to Disbursements of Compact CDF (each a “*Compact CDF Disbursement*”). Upon execution of the Program Implementation Agreement, each Compact CDF Disbursement will be subject to all of the terms of the Program Implementation Agreement, except that the conditions to each Compact CDF Disbursement will continue to be those set forth in this Annex IV.

1. Conditions Precedent to Initial Compact CDF Disbursement.

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

- (a) The Government (or MCA-Nepal) has delivered to MCC:
 - (i) an interim fiscal accountability plan acceptable to MCC; and
 - (ii) a Compact CDF procurement plan acceptable to MCC.
- (b) The Government will have enacted such regulations as necessary to implement Section 2.8 of this Compact.
- (c) The Government will have provided a schedule and procedures, acceptable in form and substance to MCC, for the disbursement of the first US\$40,000,000 of the Government Contribution.

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

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

- (a) The Government (or MCA-Nepal) has delivered to MCC the following documents, in form and substance satisfactory to MCC:
 - (i) a completed Disbursement Request, together with the applicable Periodic Reports, for the applicable Disbursement Period, all in accordance with the Reporting Guidelines;
 - (ii) a certificate of the Government (or MCA-Nepal), dated as of the date of the Compact CDF Disbursement Request, in such form as provided by MCC;

(iii) if a Fiscal Agent has been engaged, a Fiscal Agent Disbursement Certificate; and

(iv) if a Procurement Agent has been engaged, a Procurement Agent Disbursement Certificate.

(b) If any proceeds of the Compact CDF Disbursement are to be deposited in a bank account, MCC has received satisfactory evidence that (i) the Bank Agreement has been executed and (ii) the Permitted Accounts have been established.

(c) Appointment of an entity or individual to provide fiscal agent services, as approved by MCC, until such time as the Government provides to MCC a true and complete copy of a Fiscal Agent Agreement, duly executed and in full force and effect, and the fiscal agent engaged thereby is mobilized.

(d) Appointment of an entity or individual to provide procurement agent services, as approved by MCC, until such time as the Government provides to MCC a true and complete copy of the Procurement Agent Agreement, duly executed and in full force and effect, and the procurement agent engaged thereby is mobilized.

(e) MCC is satisfied that (i) the activities being funded with such Compact CDF Disbursement are necessary, advisable or otherwise consistent with the goal of facilitating the implementation of this 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-Nepal 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 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 Compact CDF Disbursement occurring after this Compact has entered into force in accordance with Article 7: MCC is satisfied that (1) MCC has received copies of any reports due from any technical consultants (including environmental auditors engaged by MCA-Nepal) for any Activity since the previous Disbursement Request, and all such reports are in form and substance satisfactory to MCC; (2) 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 Compact CDF Disbursement; (3) 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 Disbursement Period); (4)

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); (5) MCC does not have grounds for concluding that any matter certified to it in the related MCA Disbursement Certificate, the Fiscal Agent Disbursement Certificate or the Procurement Agent Disbursement Certificate is not as certified; and (vi) if any of the officers or key staff of MCA-Nepal have been removed or resigned and the position remains vacant, MCA-Nepal is actively engaged in recruiting a replacement.

(g) MCC has not determined 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, this Compact or MCC Funding in accordance with Section 5.1 of this Compact.

(h) Prior to the third Compact CDF Disbursement, the Government will have designated the Electricity Transmission Project as a National Pride Project.

(i) The Government must be in compliance with the schedules and procedures provided pursuant to Section 1(c) above.

ANNEX V

ADDITIONAL CONDITIONS PRECEDENT TO ENTRY INTO FORCE

The following additional conditions precedent must be met before this Compact enters into force.

(a) The Government must have submitted a plan, in form and substance acceptable to MCC, and consented to by the governments of India, memorializing (i) key financial and technical terms for the construction of the New Butwal-Gorakhpur cross-border transmission line, and (ii) operational principles for the New Butwal-Gorakhpur cross-border transmission line;

(b) The Government must have submitted evidence to MCC that the Electricity Regulatory Commission bill has either been passed by the Federal Parliament, or that progress, satisfactory to MCC, is being made on the passage of the bill;

(c) The Government must have completed those approvals, permits, and determinations, identified by MCC as necessary to ensure that all necessary land acquisition, site access and forest clearance is completed in a timely manner to ensure Projects may be completed prior to the Compact End Date; and

(d) The Government will have designated the Electricity Transmission Project as a National Pride Project.

ANNEX VI

DEFINITIONS

Activity has the meaning provided in Section 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).

Baseline has the meaning provided in paragraph 3 of Annex III.

BIKAS has the meaning provided in Section B.1(a)(i)(A) of Annex I.

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

Compact has the meaning provided in the Preamble.

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

Compact CDF Disbursement has the meaning provided in the preamble to Annex IV.

Compact Goal has the meaning provided in Section 1.1.

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

Compact Term has the meaning provided in Section 7.4.

COS has the meaning provided in Annex VII.

Covered Provider has the meaning provided in the Audit Guidelines.

DFID has the meaning provided in Section B.1(e) of Annex I.

Disbursement has the meaning provided in Section 2.4.

DOC has the meaning provided in Annex VII.

DOR has the meaning provided in Section A.2(a) of Annex I.

DQR has the meaning provided in paragraph 5 of Annex III.

Electricity Transmission Project has the meaning provided in Section B.1(a) of Annex I.

ERC has the meaning provided in Section B.1(a)(iii) of Annex I.

ERR has the meaning provided in paragraph E.1.a. of Annex III.

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

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

Exempt Entity has the meaning provided in Schedule A to Annex VII.

Exempt Employers has the meaning provided in Schedule E to Annex VII.

Exempt Individual has the meaning provided in Schedule A to Annex VII.

Exempt Personal Income has the meaning provided in Schedule E to Annex VII.

Fiscal Agent has the meaning provided in Section C.3 of Annex I.

Governance Guidelines means MCC's Guidelines for Accountable Entities and Implementation Structures.

Government has the meaning provided in the Preamble.

Government Contribution has the meaning provided in Section 2.6.

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

GWh has the meaning provided in Annex III.

IFC Performance Standards has the meaning provided in Section B.1(c) of Annex I.

Implementation Letter has the meaning provided in Section 3.5.

Income Tax Exempt Entity has the meaning provided in Schedule D to Annex VII.

Income Tax Exempt Individual has the meaning provided in Schedule D to Annex VII.

Indicators has the meaning provided in paragraph 3.a. of Annex III.

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

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.

Internal Regulations has the meaning provided in Section C.1(a) of Annex I.

IRD has the meaning provided in Annex VII.

IRI has the meaning provided in paragraph 1 of Annex III.

ITT has the meaning provided in paragraph 3 of Annex III.

kV has the meaning provided in paragraph 2 of Annex III.

Local Taxes has the meaning provided in Schedule K to Annex VII.

LRO has the meaning provided in Annex VII.

M&E Plan has the meaning provided in the first paragraph of Annex III.

Management Unit has the meaning provided in Section C.1(a) of Annex I.

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

MCA-Nepal has the meaning provided in Section 3.2(b).

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 such policy).

MCC M&E Policy has the meaning provided in the first paragraph of Annex III.

MCC Program Closure Guidelines means the MCC Program Closure Guidelines (including any guidance documents issued in connection with such guidelines).

MCC Program Procurement Guidelines has the meaning provided in Section 3.6.

MCC Website means the MCC website at www.mcc.gov.

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

Multi-Year Financial Plan Summary has the meaning provided in Section I of Annex II.

MW has the meaning provided in paragraph 2.1 of Annex III.

NEA has the meaning provided in Section B.1(a)(iii) of Annex I.

Nepal has the meaning provided in the Preamble.

Other National Taxes has the meaning provided in Schedule J to Annex VII.

Party and Parties have the meaning provided in the Preamble.

Pavement Recycling sub-Activity has the meaning provided in Section B.2(a)(ii) of Annex I.

Permitted Account has the meaning provided in Section 2.4.

Personal Income Taxes has the meaning provided in Schedule D to Annex VII.

Personal Tax Exempt Individual has the meaning provided in Schedule E to Annex VII.

Petroleum Taxes has the meaning provided in Schedule F to Annex VII.

Principal Representative has the meaning provided in Section 4.2.

Procurement Agent has the meaning provided in Section C.4 of Annex I.

Program has the meaning provided in the recitals to this Compact.

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 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, the MCC Gender Policy, the MCC Gender Integration Guidelines, the MCC Guidelines for Economic and Beneficiary Analysis, the MCC Standards for Global Marking, and any other guidelines, policies or guidance papers relating to the administration of MCC-funded compact programs, in each case, as such may be posted from time to time on the MCC Website.

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

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

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

Project Cooperation Agreement has the meaning provided in Section C.2 of Annex I.

Project Partner has the meaning provided in Section C.2 of Annex I.

Property Taxes has the meaning provided in Schedule H to Annex VII.

Provider means (i) 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 (ii) 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.

RBN has the meaning provided in Section A.2(a) of Annex I.

Reporting Guidelines means the MCC Guidance on Quarterly MCA Disbursement Request and Reporting Package.

Road Maintenance Project has the meaning provided in Section B.2(a) of Annex I.

SDI has the meaning provided in Annex III.

SEP has the meaning provided in Section C.1(d) of Annex I.

Service Taxes has the meaning provided in Schedule I to Annex VII.

SRN has the meaning provided in Section B.2(a) of Annex I.

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

Supplemental Agreement means any agreement between (A) the Government (or any Government affiliate, including MCA-Nepal) and MCC (including, but not limited to, the PIA), or (B) MCC and/or the Government (or any Government affiliate, including MCA-Nepal), 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 3 of Annex III.

Tax Departments has the meaning provided in Annex VII.

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

Telecommunication Taxes has the meaning provided in Schedule G to Annex VII.

VAT has the meaning provided in Annex VII.

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

USAID has the meaning provided in Section A.1(b) of Annex I.

ANNEX VII

TAX SCHEDULES

The Government will ensure that MCA-Nepal and all Providers, Covered Providers, Project Partners, contractors (prime contractors and subcontractors), consultants, and other entities and individuals that receive MCC funding directly or indirectly in furtherance of the Compact are exempt from Taxes or will be refunded equal amount of Taxes paid in respect of the MCC funding in accordance with Section 2.8.

The following Schedules identify specific Taxes and mechanisms to implement compliance with the tax exemption under the Compact. The Government will provide an instruction letter and a copy of the Compact, including these Schedules, to the Inland Revenue Department of Nepal (“*IRD*”), Department of Customs (“*DOC*”), Land Revenue Offices (“*LRO*”), Custom Offices (“*COS*”) and all other authorities, including local and state authorities, involved in tax collection and administration (collectively “*Tax Departments*”) to ensure that the Tax Departments implement the terms of the Compact and the mechanisms to implement the tax exemption as agreed herein, or as otherwise adopted under the Compact.

MCA-Nepal will facilitate and assist all other beneficiaries of the tax exemption, including Providers, Covered Providers, Project Partners, contractors (prime contractors and subcontractors), consultants, and other entities and individuals that receive MCC funding directly or indirectly in furtherance of the Compact, to ensure compliance with the exemption or refund terms herein that apply to Taxes.

There is not a need to make multiple applications or recommendations if more than one tax is required to be exempted or refunded in respect of the same transaction (e.g. value added tax (“*VAT*”), excise duty, and custom duty applying to same goods or services).

Taxes to be exempt and refunded are set out below:

Schedule	Tax	Mechanism
A	Value Added Tax	Exemption and refund
B	Custom Duties	Exemption and refund
C	Excise Duties	Exemption and refund
D	Corporate Income and Withholding Tax	Exemption
E	Individual Income Tax	Exemption
F	Taxation of Petroleum Products	Exemption and refund
G	Taxation of Telecommunication Services	Exemption and refund
H	Property Taxes	Exemption and refund
I	Service Taxes	Exemption and refund
J	Other National Taxes	Exemption and refund
K	Local Taxes	Exemption and refund

SCHEDULE A
VALUE ADDED TAX

Legal Basis for Exemption

1. Section 2.8 of the Compact.
2. Value Added Tax Act of 1996, Section 25(1).

Beneficiaries of Exemption

1. MCA-Nepal.
2. Each Project Partner, and any Provider, Covered Provider, or any other entity, including prime contractors and any subcontractors working directly with prime contractors and all natural persons, importing or providing goods, works or services in furtherance of the Compact (an “*Exempt Entity*” in the case of a legal entity or an “*Exempt Individual*” in the case of a natural person).

Procedures

1. *Summary* - Goods and services procured by MCA-Nepal or procured and supplied by any Exempt Entity or any Exempt Individual will be exempted from VAT or VAT will be refunded if it has been paid. MCA-Nepal, any Exempt Entity, or any Exempt Individual will be able to sell, purchase, or import goods and services in connection to the Compact without paying or collecting VAT. In circumstances where VAT has been paid by a beneficiary, IRD will refund VAT according to the procedures and timelines further outlined in this Schedule.
2. *Goods or services imported by MCA-Nepal, any Exempt Entity, or any Exempt Individual or goods imported on their behalf by another supplier* – VAT will not be charged for goods and services imported by MCA-Nepal, any Exempt Entity, or any Exempt Individual or by other suppliers on their behalf. MCA-Nepal, any Exempt Entity, or any Exempt Individual will not have to pay VAT on import of services in furtherance to the Compact. Upon the satisfaction of the following procedures, the relevant COS will not charge VAT applicable on such imports. The beneficiary applies to the Ministry of Finance (“*MOF*”) through MCA-Nepal to obtain a letter providing for tax exemption. MCA-Nepal then forwards the application to the MOF for the tax exemption with the following documents after which the MOF will, within five working days, issue an exemption letter:
 - application letter for exemption by beneficiary;
 - a letter from MCA-Nepal, issued in official letterhead which confirms that the goods are imported exclusively in furtherance of the Compact; and
 - purchase order or contract (if available).

Following receipt of the letter from the MOF, the beneficiary applies to the COS. Upon receipt of the following documents, the relevant COS shall not charge VAT applicable on such imports:

- application for reimbursement by beneficiary;
- a letter from the MOF, issued on official letterhead which confirms the tax exemption and requires the COS not to charge VAT;
- invoice for goods;
- purchase order or contract (if available);
- banking and payment documents; and
- transportation documents.

3. *Refund process for VAT paid* – In the event that procedures in paragraph 2 of this Schedule A are not practicable or do not apply, VAT will be refunded. MCA-Nepal, the Exempt Entity, or the Exempt Individual will obtain tax invoices from the supplier in respect of the goods or services purchased locally or tax assessment receipts in case of goods imported in respect of which VAT has been paid and apply for refund of the VAT paid along with the following documents:

- application for refund by beneficiary;
- a letter from MCA-Nepal, issued on official letterhead confirming that the goods and services are provided exclusively in furtherance of the Compact, the name of the project, the name of the beneficiary of the exemption, and the name of the supplier;
- copy of purchase order or contract (if available); and
- original tax invoice or tax receipt issued by the supplier.

IRD will refund the VAT within 30 working days upon receiving the request from the beneficiary.

SCHEDULE B
CUSTOMS DUTIES

Legal Basis for Exemption

1. Section 2.8 of the Compact.
2. Customs Act of 2007, Section 9(4)

Beneficiaries of Exemption

1. MCA-Nepal.
2. Each Exempt Entity or Exempt Individual.

Procedures

1. *Summary* – MCA-Nepal, any Exempt Entity, or any Exempt Individual, or any other person importing goods on their behalf in connection to the Compact (including goods imported temporarily) will be exempt from paying custom duty on items imported in connection to the Compact.
2. *Goods imported by MCA-Nepal, Exempt Entity, or Exempt Individual or by a supplier on their behalf* – Custom duty will not be charged for goods imported by MCA-Nepal, any Exempt Entity, or any Exempt Individual or by other suppliers on their behalf. The beneficiary applies to the MOF through MCA-Nepal to obtain a letter providing tax exemption. MCA-Nepal then forwards the application to the MOF for the tax exemption with the following documents after which the MOF will, within five working days, issue an exemption letter:
 - application letter for exemption by beneficiary;
 - a letter from MCA-Nepal, issued on official letterhead which confirms that the goods are imported exclusively in the furtherance of the Compact; and
 - purchase order or contract (if available).

Following receipt of the letter from the MOF, the beneficiary applies to the COS. Upon receipt of the following documents, the relevant COS shall not charge custom duty applicable on such imports:

- application for reimbursement by beneficiary;
- a letter from the MOF, issued in official letterhead which confirms the tax exemption and requires the COS not to charge custom duty;
- invoice for the goods;
- purchase order or contract (if available);
- banking and payment documents; and
- transportation documents.

The COS will promptly clear the goods within five working days and grant exemption from custom duties applicable on such imports.

3. *Refund for goods purchased by MCA-Nepal, Exempt Entity or Exempt Individual on which custom duty has been paid by the importer* – MCA-Nepal, any Exempt Entity, or any Exempt Individual will be entitled to refund of any custom duty applying to goods which was imported by the supplier for which supplier has paid custom duty. The beneficiary will apply to the IRD for refund of the custom duty paid along with the following documents:

- application for refund by beneficiary;
- a letter from MCA-Nepal, issued on official letterhead which confirms that the goods are provided exclusively in furtherance of the Compact, the name of the project, the name of the beneficiary of the exemption, and the name of the supplier;
- copy of purchase order or contract (if available);
- copies of documents showing custom duty paid in respect of such goods;
- original tax invoice or tax receipt issued by the supplier; and
- documents evidencing tax paid during import.

IRD will refund such duty within 30 working days of application by the beneficiary.

SCHEDULE C
EXCISE DUTIES

Legal Basis for Exemption

1. Section 2.8 of the Compact.

Beneficiaries of Exemption

1. MCA-Nepal.
2. Each Exempt Entity or Exempt Individual.

Procedures

1. *Summary* - Goods and services procured by MCA-Nepal, any Exempt Entity, or any Exempt Individual will be exempted from excise duties or will be refunded. MCA-Nepal, any Exempt Entity, or any Exempt Individual will be able to purchase or import goods and services without paying excise duty during production or import.
2. *Goods imported by MCA-Nepal, Exempt Entity, or Exempt Individual or by a supplier on their behalf* - Excise duty will not be charged for goods imported by MCA-Nepal, any Exempt Entity, or any Exempt Individual or by other suppliers on their behalf. The beneficiary applies to the MOF through MCA-Nepal to obtain a letter providing tax exemption. MCA-Nepal then forwards the application to the MOF for the tax exemption with the following documents after which the MOF will, within five working days, issue an exemption letter:
 - Application letter for exemption by beneficiary;
 - a letter from MCA-Nepal, issued on official letterhead which confirms that the goods are imported exclusively in furtherance of the Compact; and
 - purchase order or contract (if available).

Following receipt of the letter from the MOF, the beneficiary applies to the COS. Upon receipt of the following documents, the relevant COS shall not charge excise duty applicable on such imports:

- application for reimbursement by beneficiary;
- a letter from the MOF, issued on official letterhead which confirms the tax exemption and requires the COS not to charge excise duty;
- invoice for the goods;
- purchase order or contract (if available);
- banking and payment documents; and
- transportation documents.

The COS will promptly clear the goods within five working days and grant exemption from excise duties applicable on such imports.

3. *Duty exemption for local goods and services purchased by or for MCA-Nepal, Exempt Entity, or Exempt Individual* – For locally produced goods or services for which excise duty is applicable, purchased by or supplied to MCA-Nepal, any Exempt Entity, or Exempt Individual will be exempt from excise duty. The beneficiary will submit the following documents to the IRD in respect of goods and services for which exemption from excise duty should apply:

- application for exemption by beneficiary;
- a letter from MCA-Nepal, issued on official letterhead which confirms that the goods and services are provided exclusively in furtherance of the Compact, the name of the project, the name of the beneficiary of the exemption, and the name of the supplier;
- two copies of the pro forma invoice issued by the supplier;
- copy of purchase order or contract (if available); and
- tax registration certificate of the supplier.

The IRD, within five working days of receipt the above documents, will stamp the pro forma invoice submitted and issue an exemption certificate. On receipt of such stamped pro forma invoice, the supplier will supply goods and services without charging excise duty.

SCHEDULE D

CORPORATE INCOME AND WITHHOLDING TAX

Legal Basis for Exemption

1. Section 2.8 of the Compact.
2. Income Tax Act 2002 Section 10(a).

Beneficiaries of Exemption

1. MCA-Nepal.
2. Each Exempt Entity, other than legal persons that are legal entities registered under the laws of Nepal (the “*Income Tax Exempt Entity*”). Any income that is derived from MCC funding by legal entities or persons, but not individuals, that are considered taxable, per the tax code, due to residence in Nepal solely with respect to their work performed in furtherance of the Compact will not be considered taxable or subject to taxation in Nepal.

Procedures

1. MCA-Nepal and all Income Tax Exempt Entities will be entitled to an exemption from Nepali income tax and related taxes on income earned from supplying goods, works, or services in furtherance of the Compact.
2. MCA-Nepal will not be required to withhold tax deductible at source from payments made from or with respect to MCC Funding to an Income Tax Exempt Entity.
3. Income Tax Exempt Entities will not be required to withhold tax deductible at source from payments made from or with respect to MCC Funding when purchasing goods, works, or service in furtherance of the Compact.
4. Income Tax Exempt Entities not registered under the laws of Nepal that may have permanent establishment in Nepal will register as a taxable person in Nepal. MCA-Nepal will arrange this registration with a tax office of the IRD so that the Income Tax Exempt Entity (including its permanent establishment) and all income derived from MCC Funding will be exempt from taxation.
5. All income derived from MCC Funding will be recorded as exempt income and an Income Tax Exempt Entity will not be liable to pay tax with respect to any such income, including any taxes in respect to transfer of such income.
6. Entities other than Income Tax Exempt Entities deriving their income from MCC funding will themselves be responsible for filing their own tax returns and paying their taxes.

SCHEDULE E
INDIVIDUAL INCOME TAX

Legal Basis for Exemption

1. Section 2.8 of the Compact.
2. Income Tax Act 2002 Section 10(a).

Beneficiaries of Exemption

All natural persons, whether paid internally or externally, working in furtherance of the Compact (each “*Income Tax Exempt Individual*”), other than citizens or residents of Nepal. Persons who derive income hereunder who otherwise were not citizens or residents of Nepal prior to receiving that income will also be deemed Income Tax Exempt Individuals.

Procedures

1. The Income Tax Exempt Individuals will be exempt from any income, social security, medical insurance, provident funds, or other mandatory taxes and charges imposed by Nepal on personal income (the “*Personal Income Taxes*”) received in connection with income earned from works and services performed in furtherance of the Compact (the “*Exempt Personal Income*”)
2. MCA-Nepal, the Exempt Entities, the Fiscal Agent and the Procurement Agent and any other vendor (the “*Exempt Employers*”) who employs Income Tax Exempt Individuals will not withhold or pay Personal Income Taxes for the Income Tax Exempt Individuals.
3. The Income Tax Exempt Individuals will have no obligation to file an income tax return in Nepal in relation to the Exempt Personal Income.
4. The Exempt Employers will have no obligation under the laws of Nepal in connection with the completion of any filings, registrations or reporting in relation to the Exempt Personal Income of the Income Tax Exempt Individuals.
5. Persons other than Income Tax Exempt Individuals deriving their income from MCC funding will themselves be responsible for filing their own tax returns and paying their taxes.

SCHEDULE F

TAXATION OF PETROLEUM PRODUCTS

Legal Basis for Exemption

1. Section 2.8 of the Compact.

Beneficiaries of Exemption

1. MCA-Nepal.
2. Each Exempt Entity or Exempt Individual.

Procedures

1. *Overview* - MCA-Nepal, any Exempt Entity, or any Exempt Individual will be exempted from customs duty, excise duty, pollution control fee, infrastructure tax, and all other taxes and duties applicable on petroleum products (“*Petroleum Taxes*”) or any Petroleum Tax paid by the beneficiaries will be refunded.
2. *Petroleum purchased from Nepal Oil Corporation in bulk* - MCA-Nepal will facilitate the registration and purchasing of petroleum products wholesale or in bulk, including providing any necessary certifications to permit beneficiaries under this Schedule to make purchases. Following application by MCA-Nepal, the MOF will write to the Nepal Oil Corporation (directly or through the Ministry of Suppliers, as appropriate) within five working days to provide petroleum products on a duty free basis to the beneficiaries. Nepal Oil Corporation will be exempted from paying any Petroleum Taxes on the products supplied to the beneficiaries on a duty free basis. The beneficiary will submit the following documents to the Nepal Oil Corporation in order to receive exemption from Petroleum Taxes:
 - application for exemption by beneficiary;
 - a letter from MCA-Nepal, issued on official letterhead which confirms that the goods and services are provided exclusively in furtherance of the Compact, the name of the project, the name of the beneficiary of the exemption;
 - a letter from the MOF, issued on official letterhead which confirms the tax exemption and requires the relevant authorities not to charge taxes; and
 - copy of purchase order or contract (if available).
3. *Non-bulk purchase made from retail outlets* – Petroleum Taxes paid in respect of products purchased from retail outlets will be refunded. MCA-Nepal, any Exempt Entity, or any Exempt Individual will obtain from the local supplier any invoices and/or receipts relating to the Petroleum Tax in respect of the petroleum products in which Petroleum Taxes have been paid. The beneficiary will apply to the IRD for refund of the Petroleum Taxes paid along with the following documents:

- application for refund by beneficiary;
- a letter from MCA-Nepal, issued on official letterhead which confirm that the petroleum products are provided exclusively in furtherance of the Compact, the name of the project, the name of the beneficiary of the exemption, and the name of the supplier;
- original tax invoice or tax receipt issued by the supplier; and
- breakdown of Petroleum Tax paid in respect of the retail purchase.

The IRD will refund to the beneficiary the Petroleum Taxes paid within 30 working days of receipt of the application for refund.

SCHEDULE G

TAXATION OF TELECOMMUNICATION SERVICES

Legal Basis for Exemption

1. Section 2.8 of the Compact.

Beneficiaries of Exemption

1. MCA-Nepal.
2. Each Exempt Entity or Exempt Individual.

Procedures

1. *Overview* - MCA-Nepal, any Exempt Entity or any Exempt Individual will be exempted from telecommunication ownership fee, telecommunication service fee, value added tax, and all other taxes and duties applying to telecommunication services (“*Telecommunication Taxes*”) or be refunded

2. *Exemption from Telecommunication Taxes* - MCA-Nepal, any Exempt Entity, or any Exempt Individual will be exempt from all Telecommunication Taxes. Following application by MCA-Nepal, the MOF shall write to the IRD confirming the exemption. The beneficiary will submit the following documents to the IRD in respect of telecommunication services for which exemption should apply:

- application for exemption by beneficiary;
- a letter from MCA-Nepal, issued on official letterhead which confirms that the telecommunication services are provided exclusively in furtherance of the Compact, the name of the project, the name of the beneficiary of the exemption, and the name of the supplier;
- a letter from the MOF confirming the tax exemption;
- two copies of pro forma invoice issued by the service provider;
- copy of purchase order or contract (if available); and
- tax registration certificate of the service provider.

The IRD, within five working days of receipt the above documents, will stamp the pro forma invoice submitted and issue an exemption certificate. On receipt of such stamped pro forma invoice, the beneficiary will be exempt and the telecommunication service provider will not charge any Telecommunication Taxes on the services it provides to the beneficiary.

3. *Refund of Telecommunication Taxes* - In the event that procedures in paragraph 2 of this Schedule G are not practicable or do not apply, Telecommunication Taxes paid in respect of services purchased will be refunded. MCA-Nepal, any Exempt Entity, or any Exempt Individual will obtain from the local supplier in respect of the telecommunication services in which Telecommunication Taxes have been paid. Following application by

MCA-Nepal, the MOF shall write to the IRD confirming the exemption. The beneficiary will apply to the IRD for refund of the Telecommunication Taxes paid along with the following documents:

- application for refund by beneficiary;
- a letter from MCA-Nepal, issued on official letterhead which confirms that the services are provided exclusively in furtherance of the Compact, the name of the project, the name of the beneficiary of the exemption, and the name of the service provider;
- a letter from the MOF confirming the tax exemption;
- original tax invoice or recharge cards issued by the service provider; and
- breakdown of Telecommunication Taxes applicable on such invoice.

The IRD will refund to the beneficiary the Telecommunication Taxes paid within 10 working days of receipt of the application for refund.

SCHEDULE H
PROPERTY TAXES

Legal Basis for Exemption

1. Section 2.8 of the Compact.

Beneficiaries of Exemption

1. MCA-Nepal.
2. Each Exempt Entity or Exempt Individual.

Procedures

1. *Overview* - MCA-Nepal, any Exempt Entity, or any Exempt Individual will be exempted from registration fee, service fee, charge fees, and all forms of taxes applicable on ownership, transfer of ownership, mortgage of land, houses, properties, and registration of legal documents relating to property ("***Property Taxes***").
2. *Exemption from Property Taxes* - MCA-Nepal will write to the relevant Government department in charge of the collection of Property Taxes to exempt MCA-Nepal, any Exempt Entities, and any Exempt Individuals from Property Taxes. Following application by MCA-Nepal, the MOF shall issue a letter confirming the exemption. The beneficiary will submit the following documents in respect of Property Taxes for which exemption should apply to the LRO or Tax Departments:
 - application for exemption by beneficiary; and
 - a letter from MCA-Nepal, issued on official letterhead which confirms that the transaction is undertaken exclusively in furtherance of the Compact, the name of the project, and the name of the beneficiary of the exemption;
 - a letter from the MOF confirming the tax exemption; and
 - other documents setting out the nature of the transaction for which Property Taxes apply (if applicable).

The LRO or Tax Departments in charge of collecting such taxes will exempt the beneficiaries from paying any Property Taxes after receiving the documents.

SCHEDULE I
SERVICE TAXES

Legal Basis for Exemption

1. Section 2.8 of the Compact.

Beneficiaries of Exemption

1. MCA-Nepal.
2. Each Exempt Entity or Exempt Individual.

Procedures

1. MCA-Nepal, any Exempt Entity, or any Exempt Individual will be exempted from taxes, including health services tax, education services tax, and all other taxes or duties applicable on the sale of products and services (“*Service Taxes*”).
2. *Tax exemption for goods and services purchased by MCA-Nepal, Exempt Entity, or Exempt Individual* – MCA-Nepal, any Exempt Entity or any Exempt Individual will be exempt from all Service Taxes. Following application by MCA-Nepal, the MOF shall write to the IRD confirming the exemption. The beneficiary will submit the following documents to the IRD in respect of goods or services for which exemption should apply:
 - application for exemption by beneficiary;
 - a letter from MCA-Nepal, issued on official letterhead which confirms that the goods or services are provided exclusively in furtherance of the Compact, the name of the project, the name of the beneficiary of the exemption, and the name of the supplier;
 - a letter from the MOF confirming the tax exemption;
 - two copies of the pro forma invoice issued by the supplier;
 - copy of purchase order or contract (if available); and
 - tax registration certificate of the supplier.

The IRD, within five working days of receipt the above documents, will stamp the pro forma invoice submitted and issue an exemption certificate. On receipt of such stamped pro forma invoice, the beneficiary will be exempt and the service provider will not charge any Service Taxes on the goods or services it provides to the beneficiary.

3. *Goods and services locally purchased by MCA-Nepal, Exempt Entity or Exempt Individual*– In the event that procedures in paragraph 2 of this Schedule I are not practicable or do not apply, MCA-Nepal, any Exempt Entity, or any Exempt Individual will obtain from the local supplier invoices relating to payment of Service Taxes in respect of the goods purchased in which Service Taxes has been paid. Following application by MCA-Nepal, the MOF shall write to the IRD confirming the exemption.

The beneficiary will apply to the IRD for refund of the Service Taxes paid along with the following documents:

- application for refund by beneficiary;
- a letter from MCA-Nepal, issued on official letterhead which confirms that the services are provided exclusively in furtherance of the Compact, the name of the project, the name of the beneficiary of the exemption, and the name of the service provider;
- a letter from the MOF confirming the tax exemption; and
- original tax invoice issued by the supplier.

The IRD will refund to the beneficiary the Service Taxes paid within 10 working days of receipt of the application for refund.

SCHEDULE J
OTHER NATIONAL TAXES

Legal Basis for Exemption

1. Section 2.8 of the Compact.

Beneficiaries of Exemption

1. MCA-Nepal.
2. Each Exempt Entity or Exempt Individual.

Procedures

1. *Overview* - MCA-Nepal, any Exempt Entity, or any Exempt Individual will be exempted from all other national taxes imposed by the Federal Government of Nepal not covered in Schedules A to I of Annex VII ("**Other National Taxes**").
2. *Exemption of Other National Taxes* - For matters for which Other National Taxes are applicable, MCA-Nepal will write the relevant authority collecting the tax to exempt MCC Funding or beneficiaries of such funding from the requirement. Such taxes will be exempted by such authorities based on an official letter from the MOF obtained by the beneficiary by applying through the MCA-Nepal. The official letter will be provided to the relevant Tax Department assessing or collecting the tax in order to justify the exemption.
3. *Refund of Other National Taxes*– In the event that procedures in paragraph 2 of this Schedule J are not practicable or do not apply, MCA-Nepal, Exempt Entity or Exempt Individual will obtain the invoice or receipt in respect of which Other National Taxes have been paid. The beneficiary will write to IRD with a copy of the receipt or invoice and supporting letter from MCA-Nepal and the MOF to obtain the refund of Other National Taxes. IRD will refund such taxes within 10 working days of the request.

SCHEDULE K
LOCAL TAXES

Legal Basis for Exemption

1. Section 2.8 of the Compact.

Beneficiaries of Exemption

1. MCA-Nepal, Exempt Entities, and Exempt Individuals, performing an act or action in furtherance of the Compact that triggers payment of any real property tax, business tax, regional tax, municipal tax, village tax, community tax, or other local tax under Nepali law, and any other tax other than those addressed in Schedules A through Schedule J of this Annex VII (the “*Local Taxes*”).

Procedures

1. *Overview* - MCA-Nepal, any Exempt Entity, or any Exempt Individual will be exempted from all Local Taxes.
2. *Exemption of Local Taxes* - For matters for which Local Taxes are applicable, MCA-Nepal will write the relevant authority collecting the tax to exempt MCC Funding or beneficiaries of such funding from the requirement. Such taxes will be exempted by such authorities based on an official letter from the MOF obtained by the beneficiary by applying through the MCA-Nepal. The official letter will be provided to the relevant Tax Department assessing or collecting the tax in order to justify the exemption.
3. *Refund of Local Taxes*– In the event that procedures in paragraph 2 of this Schedule K are not practicable or do not apply, MCA-Nepal, Exempt Entity or Exempt Individual will obtain the invoice or receipt in respect of which Local Taxes have been paid. The beneficiary will write to IRD with a copy of the receipt or invoice and supporting letter from MCA-Nepal and the MOF to obtain the refund of Local Taxes. IRD will refund such taxes within 10 working days of the request.