ADDENDUM NO 3 TO THE ADMINISTRATION AGREEMENT FOR EUROPEAN UNION CONTRIBUTIONS, AS REPRESENTED BY THE EUROPEAN COMMISSION, TO TRUST FUNDS

World Bank Group Trust Fund No TF071410
“Economic Analysis Programme for Growth and Sustainable Development”
European Commission Trust Fund No 2009/217-942

The European Union, represented by the European Commission, B-1049 Brussels, Belgium, in order to support the economic development of the Turkish Cypriot community, in accordance with Council Regulation 389/2006 (OJ [2006] L 65/5) (the "European Commission"), on the one part,

and

The World Bank, Europe and Central Asia Region, H12-1202, 600-19th Street, NW, Washington, DC 20433 (the "World Bank"), on the other part,

have agreed as follows:

The following provisions of the Administration Agreement No 2009/217-942 “Economic Analysis Programme for Growth and Sustainable Development”, concluded between the European Commission and the World Bank on 14/12/2009 (the "Agreement"), are hereby replaced as follows:

**Article 2 Entry into force and Implementation Period**

**Section 2.03** It is expected that the Contribution will be fully utilized in accordance with the provisions of this Administration Agreement by **December 15, 2014** (“End Disbursement Date”). The End Disbursement Date can only be modified with the agreement of both Parties pursuant to Article 9 of the General Conditions.

**Article 4 Payment schedule and reporting**

**Section 4.02** Narrative progress report(s) and financial information shall be provided consistent with Article 2 of the General Conditions, and in accordance with the following schedule

- a narrative progress report shall accompany every request for a further instalment of financing.

As of entry into force of Addendum 3 to the Administration Agreement, a narrative progress report should be submitted at least once per year. A final narrative report shall be forwarded to the Commission within six (6) months after the End Disbursement Date.
- the progress financial information shall be made available via the Bank's Trust Funds Donor Centre secure website following the signature of this Administration Agreement. The final financial information shall be made available via the Bank's Trust Funds Donor Centre secure website within six (6) months after the End Disbursement Date.”

**Article 5 Communication and addresses**

Any communication relating to this Administration Agreement shall be in writing, shall state the number and title of the trust fund, and shall use the following addresses.

Payment requests and attached reports, including requests for changes to bank account arrangements pursuant to Section 9.02 of the General Conditions, shall be sent to:

For the Commission:
Head of Unit E3 – Finance and Contracts
DG Enlargement
Loi-15 06/099
B-1049 Brussels

Copies of the documents referred to above, and correspondence of any other nature, shall be sent to:

European Commission
Ms Michaela Di Bucci
Head of Unit 02 – Task Force Turkish Cypriot community
DG Enlargement
Loi-15 11/039
B-1049 Brussels

And also by e-mail to:
Sara.SANGOI@ec.europa.eu.

**Article 6 Annexes**

**Section 6.01** The new versions of Annex I "Description of the Project" and Annex III "Indicative budget for the project" are attached to this addendum.

All other terms and conditions of the Administration Agreement and its previous addenda remain unchanged. This addendum shall form an integral part of the Administration Agreement and it shall enter into force on the later date of signature by the Parties.
This addendum is drawn up in three originals, two for the European Commission and one for the World Bank Group entity.

For the World Bank:

Name: Dirk Reinersmann
Position: Program Manager Southern Europe
Signature:
Date: 14/12/2013

For the European Commission:

Name: Michaela DI BUCCI
Position: Head of Unit A02 – Task Force Turkish Cypriot community
Signature:
Date: 12/12/2013
DESCRIPTION OF THE PROJECT

The following is a description of the activities to be carried out under the trust fund, subject to such minor modifications as the Commission and the Bank may mutually agree from time to time by notice in writing provided that such modifications do not materially affect the scope of the activities and the objectives of the Project.

Title

Economic Analysis Programme for Growth and Sustainable Development

Location

Northern part of Cyprus

Cost of the Action and Contribution from the Contracting Authority

<table>
<thead>
<tr>
<th>Total eligible cost of the action</th>
<th>Total contribution from the Contracting Authority</th>
</tr>
</thead>
<tbody>
<tr>
<td>EUR 1,000,000</td>
<td>EUR 1,000,000</td>
</tr>
</tbody>
</table>

Summary

Duration of the action

It is expected that the Contribution will be fully utilized in accordance with the provisions of this Administration Agreement by the End Disbursement Date.

Objectives of the action

Overall objective:

The overall objective is to assist with the development process to further economic convergence within Cyprus in view of the integration of the Cyprus economy and the on-going talks on reunification.

Specific objectives:

- To fill knowledge gaps of macroeconomic developments in the northern part of Cyprus;
- To elaborate for the Turkish Cypriot economy a reform
Objectives of the Programme

The Economic Analysis Programme for Growth and Sustainable Development is being funded through the aid regulation “Council Regulation (EC) No. 389/2006” of 27 February 2006. The first stated overall objective of the aid regulation is that “[t]he Community shall provide assistance to facilitate the reunification of Cyprus by encouraging the economic development of the Turkish Cypriot community with particular emphasis on the economic integration of the island, on improving contacts between the two communities and with the EU, and on preparation for the acquis”.

The overall objective of the Economic Analysis Programme for Growth and Sustainable Development is to assist with the development process to further economic convergence within Cyprus, with particular emphasis on the economic integration and having regard to the discussions on reunification. In this context, the specific objectives of the programme are to: (i) Fill knowledge gaps of macroeconomic developments in the northern part of Cyprus; (ii) Elaborate for the Turkish Cypriot economy, a reform agenda for selected priority areas based upon economic and sector analyses; and (iii) Enhance local understanding of constraints impeding development and reforms through dissemination of key outputs, intensive outreach and consultation.

Scope of the Programme and Description of Activities

The scope of the analytical economic programme proposed is as follows:
Stocktaking of macroeconomic and structural developments

An overview of economic developments in the northern part of Cyprus over the years 2006-2010 will be carried out to provide the economic context in which the economic and sector work (ESW) programme will be carried out. The report relies upon available data. Furthermore, the stocktaking exercise provides a basis for discussions on the economy with various stakeholders and the discussion of the elements of a meaningful reform agenda. Consequently, the main issues impacting growth will be covered including public finance and private sector development.

Macroeconomic monitoring reports

This activity will provide an annual update on economic growth, prices and exchange rates, external sector, and the general public sector budget. If feasible, any regulatory changes with a significant economic impact will also be highlighted. The macroeconomic monitoring notes (3) are primarily descriptive in nature and will not involve new analytical work. Furthermore, the monitoring reports provide information on the economic developments as measured through the most recent available data.

Live database

A “Live Database” will be established and a basic RMSM-X model will be developed and handed over to the beneficiaries in order for it to be used for future macroeconomic monitoring as well as the basis for any fiscal sustainability work. The Live database will be an excel-based database of key macroeconomic indicators that would be used to feed into the RMSM-X model. The RMSM-X model (Revised Minimum Standard Model Extended) is a macroeconomic simulation tool for analysing macroeconomic policies and financial flows of developing countries. It models the economy using a comprehensive flow-of-funds framework. A basic model includes the National Accounts, Public Sector, Monetary Sector, and a 'Rest of the Economy Account'.

The Live database will be handed over along with a (macroeconomic) review that utilizes the outputs from the macro model and data from other sources to provide recommendations for policy action on important macroeconomic issues. This report will include analytical results from the RMSM-X model regarding the economic effects of various plausible macroeconomic policies and financial flows.

Public Expenditure Review (PER)

The PER will analyze the public finance management system, especially in the face of annual deficits. Particular attention will also be paid to requirements for restructuring fiscal management to accord with the requirements of the acquis. In broad terms, the PER will undertake the analysis of the following topics: (i) on the side of expenditures, assistance will be provided on expenditure management which has the objective of increasing compatibility with requirements of the acquis; (ii) restructuring revenue raising to reduce incompatibility with the acquis; (iii) stocktaking of non-financial public enterprises and the fiscal burden and (iv) sustainability of the pension system. In light of the importance if this report for Cyprus, a wide dissemination effort is planned for this specific report beyond the usual dissemination planned for each and every of them. The team plans to hold a workshop with the administration in the Northern part of the Island and inviting a broad array of stake holders to discuss the findings of the report. Follow-up presentations of the findings to Universities, think tanks and other interested parties on a bi-lateral basis would also be part of the dissemination effort.
Financial Sector Review

One of the primary objectives of the financial sector review will be the development of actionable recommendations for the reform of the financial sector in the northern part of Cyprus. To ensure the medium-term stability of the economy’s financial system, it will be important to determine what the strains on the financial sector are and whether any particular aspects of it need to be strengthened at an institutional level or at the policy level. The main components of the financial sector review will focus on the banking sector. Five areas of analysis will provide the focal point of this exercise: (i) systemic and solvency analysis which includes stress testing, analysis of financial soundness indicators, and macro financial linkages; (ii) analysis of financial sector structure covering the characteristics of efficiency, competitiveness, concentration, and liquidation; (iii) assessment of observance and implementation of relevant international standards, codes, and good practices; (iv) analysis of specific stability and development issues tailored to economy circumstances and (v) assessment of asset and/or liquidity position of specific institutions.

Competitiveness

In view of the integration of the economy of Cyprus, the on-going talks on reunification and the need to increase opportunities for employment, this study will: (i) identify policy areas to promote greater economic dynamism and enhance competitiveness. Analysis will focus on policies affecting the supply-side sources of growth – labour, capital investment, and total factor productivity. The objective is to assess selected measures to foster greater private sector development to improve conditions for reunification and to accelerate income convergence between the Turkish Cypriot and Greek Cypriot communities. A better understanding of these issues and the trade integration analysis in (iii) below will also be important in the context of the eventual application of the acquis’s four freedoms – movement of labour, capital, goods, and services. (ii) Elaborate a strategy for institutional strengthening to improve public-private sector consultation. The goal is to find ways to enhance the provision of public inputs to existing private sector activities with the aim to improve productivity and product quality. (iii) Identify barriers to expanding international trade integration. The goal is to assess the impact of the current foreign trade regime and important aspects of the business climate on the volume and pattern of trade with a view toward improving the conditions for trade expansion in response to reunification and an enlarged opening to EU markets.

Policy Notes

The economic analytical programme will include five policy notes which will be short documents that answer specific questions by providing an economic analysis and relevant international experience. These policy notes can be especially useful for analysing the economic impact of specific reforms. The policy notes will be characterized by both the specificity of the topic as well as the resources devoted to the product. One of the policy notes is underway and will look at the opportunities and the constraints to further benefits from “Green Line Trade”. The other policy notes will be defined in due course with the counterparts.

Team Proposed for the Implementation

It is anticipated that the team will be led by Francis Rowe under the supervision of Dirk Reinerman (Manager Southern Europe), Satu Kahkonen (Sector Manager). The team leaders of individual studies will include Thomas Laursen and Karlis Smits (Public Finance Review), John Pollner (financial sector), Francis Rowe and Anil Onal (macroeconomic monitoring), Bart Kaminsky (Green Line Trade) and Mariana Iooty (competitiveness). Additional World Bank staff and consultants will be identified to participate in various tasks.
The World Bank may change the personnel assigned to the supervision or the team, as required.

Timetable of Activities

The programme will be implemented over three years. The estimated dates of the submission of the draft reports for review to the EU from the World Bank are as follows:

- Stocktaking of macroeconomic and structural developments (May 2012);
- Macroeconomic monitoring notes, annual basis (May 2012, December 2013, and October 2014);
- Live Data Base – RMSM-X - (December 2014)
- Financial Sector Review (October 2013);
- Public Expenditure Review (December 2013);
- Global Competitiveness study (March 2014);
- Policy note series (5 notes) (unspecified timetable during January 2014 – December 2014)
Annex III of the Administration Agreement 2009/217-942
Indicative budget for the project November 2013

<table>
<thead>
<tr>
<th>Activities &amp; Components Cost Breakdown</th>
<th>Original budget</th>
<th>Addendum 1</th>
<th>Addendum 3</th>
</tr>
</thead>
<tbody>
<tr>
<td>Conception report</td>
<td>6.675,00</td>
<td>0,00</td>
<td>0,00</td>
</tr>
<tr>
<td>Stocktaking of macroeconomic and structural developments</td>
<td>187.165,00</td>
<td>220.576,00</td>
<td>222.279,00</td>
</tr>
<tr>
<td>Macroeconomic monitoring of recent developments on a semi-annual basis using available data</td>
<td>137.008,00</td>
<td>51.139,00</td>
<td>0,00</td>
</tr>
<tr>
<td>Macroeconomic monitoring (3 annual notes)</td>
<td>0,00</td>
<td>0,00</td>
<td>85.000,00</td>
</tr>
<tr>
<td>Macroeconomic modeling</td>
<td>0,00</td>
<td>192.593,00</td>
<td>0,00</td>
</tr>
<tr>
<td>Live Data Base</td>
<td>0,00</td>
<td>0,00</td>
<td>30.000,00</td>
</tr>
<tr>
<td>Financial Sector Review</td>
<td>217.475,00</td>
<td>129.879,00</td>
<td>189.401,00</td>
</tr>
<tr>
<td>Global Competitiveness</td>
<td>150.122,00</td>
<td>118.423,00</td>
<td>150.000,00</td>
</tr>
<tr>
<td>Policy Notes (5)</td>
<td>172.671,00</td>
<td>120.366,00</td>
<td>120.000,00</td>
</tr>
<tr>
<td>Media &amp; Workshop costs</td>
<td>45.564,00</td>
<td>83.704,00</td>
<td>120.000,00</td>
</tr>
<tr>
<td>Total Direct Cost of the Contribution</td>
<td>916.680,00</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Indirect Costs (3% of the Direct Cost of the Contribution)</td>
<td>30.000,00</td>
<td>30.000,00</td>
<td>30.000,00</td>
</tr>
<tr>
<td>TF Administration</td>
<td>22.122,00</td>
<td>22.122,00</td>
<td>22.122,00</td>
</tr>
<tr>
<td>TF Program Management</td>
<td>31.198,00</td>
<td>31.198,00</td>
<td>31.198,00</td>
</tr>
<tr>
<td>TOTAL</td>
<td>1.000.000,00</td>
<td>1.000.000,00</td>
<td>1.000.000,00</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Expense Categories</th>
<th>Amount in EUR</th>
<th>Amount in EUR</th>
<th>Amount in EUR</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Staff Costs</td>
<td>440.771,00</td>
<td>356.240,00</td>
<td>468.222,00</td>
</tr>
<tr>
<td>2. Associated Overheads</td>
<td>25.243,00</td>
<td>25.243,00</td>
<td>25.243,00</td>
</tr>
<tr>
<td>3. Consultant fees</td>
<td>82.618,00</td>
<td>180.797,00</td>
<td>200.000,00</td>
</tr>
<tr>
<td>4. Contractual Services</td>
<td>34.351,00</td>
<td>192.593,00</td>
<td>25.000,00</td>
</tr>
<tr>
<td>5. Media &amp; Workshop costs</td>
<td>10.305,00</td>
<td>14.815,00</td>
<td>50.000,00</td>
</tr>
<tr>
<td>6. Travel Expenses</td>
<td>332.055,00</td>
<td>174.387,00</td>
<td>193.832,00</td>
</tr>
<tr>
<td>7. Extended Term Consultants</td>
<td>41.222,00</td>
<td>22.221,00</td>
<td>4.000,00</td>
</tr>
<tr>
<td>8. Temporary Support Staff Costs</td>
<td>3.435,00</td>
<td>3.704,00</td>
<td>3.703,00</td>
</tr>
<tr>
<td>9. Indirect Costs</td>
<td>30.000,00</td>
<td>30.000,00</td>
<td>30.000,00</td>
</tr>
<tr>
<td>TOTAL:</td>
<td>1.000.000,00</td>
<td>1.000.000,00</td>
<td>1.000.000,00</td>
</tr>
</tbody>
</table>