

LOAN NUMBER 3164 PH

Project Agreement

(Energy Sector Project)

among

INTERNATIONAL BANK FOR RECONSTRUCTION
AND DEVELOPMENT

PNOC ENERGY DEVELOPMENT CORPORATION

and

PETRON CORPORATION

Dated March 16, 1990

LOAN NUMBER 3164 PH

PROJECT AGREEMENT

AGREEMENT, dated March 16, 1990, among INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT (the Bank) and PNOC ENERGY DEVELOPMENT CORPORATION (PNOC-EDC) and PETRON CORPORATION (PETRON), respectively.

WHEREAS (A) by the Loan Agreement of even date herewith between Philippine National Oil Company (the Borrower) and the Bank, the Bank has agreed to make available to the Borrower an amount in various currencies equivalent to one hundred fifty million dollars (\$150,000,000), on the terms and conditions set forth in the Loan Agreement, but only on condition that PNOC-EDC and PETRON agree to undertake such obligations toward the Bank as are set forth in this Agreement;

(B) by a subsidiary loan agreement to be entered into between the Borrower and PNOC-EDC, part of the proceeds of the loan provided for under the Loan Agreement will be made available to PNOC-EDC on the terms and conditions set forth in said Subsidiary Loan Agreement;

(C) by a subsidiary loan agreement to be entered into between the Borrower and PETRON's part of the proceeds of the loan provided for under the Loan Agreement will be made available to PETRON on the terms and conditions set forth in said Subsidiary Loan Agreement; and

WHEREAS PNOC-EDC and PETRON, in consideration of the Bank's entering into the Loan Agreement with the Borrower, has agreed to undertake the obligations set forth in this Agreement;

NOW THEREFORE the parties hereto hereby agree as follows:

ARTICLE I

Definitions

Section 1.01. Unless the context otherwise requires, the several terms defined in the Loan Agreement, the Preamble to this Agreement and the General Conditions (as so defined) have the respective meanings therein set forth.

ARTICLE I

Execution of the Project

Section 2.01. (a) PNOC-EDC and PETRON declare their commitment to the objective of the Project as set forth in Schedule 2 to the Loan Agreement, and, to this end, shall carry out Part A (1) and (2) of the Project respectively with due diligence and efficiency and in conformity with appropriate administrative, financial, engineering and industry practices, and shall provide, or cause to be provided, promptly as needed, the funds, facilities, services and other resources required for the Project.

(b) Without limitation upon the provisions of paragraph (a) of this Section and except as the Bank, PNOC-EDC and PETRON shall otherwise agree, PNOC-EDC and PETRON shall carry out Part A (1) and (2) respectively of the Project in accordance with the Implementation Program set forth in Schedule 2 to this Agreement.

Section 2.02. Except as the Bank shall otherwise agree, procurement of the goods, works and consultants' services required for Part A of the Project and to be financed out of the proceeds of the Loan shall be governed by the provisions of Schedule 1 to this Agreement.

Section 2.03. PNOC-EDC and PETRON shall carry out the obligations set forth in Sections 9.04, 9.05, 9.06, 9.07, 9.08 and 9.09 of the General Conditions (relating to insurance, use of goods and services, plans and schedules, records and reports, maintenance and land acquisition, respectively) in respect of the Project Agreement and Part A (1) and (2) of the Project, respectively.

Section 2.04. PNOC-EDC and PETRON shall duly perform all their obligations under their respective Subsidiary Loan Agreements. Except as the Bank shall otherwise agree, PNOC-EDC and PETRON shall not take or concur in any action which would have the effect of amending, abrogating, assigning or waiving of their respective Subsidiary Loan Agreements or any provision thereof.

Section 2.05. (a) PNOC-EDC and PETRON shall, at the request of the Bank, exchange views with the Bank with

regard to progress of Part A (1) and (2) of the Project, the performance of their obligations under this Agreement and under their respective Subsidiary Loan Agreements, and other matters relating to the purposes of the Loan.

(b) PNOC-EDC and PETRON shall promptly inform the Bank of any condition which interferes or threatens to interfere with the progress of Part A (1) and (2) of the Project, the accomplishment of the purposes of Loan, or the performance by PNOC-EDC and PETRON of their obligations under this Agreement and under their respective Subsidiary Loan Agreements.

ARTICLE III

Management and Operations of PNOC-EDC and PETRON

Section 3.01. PNOC-EDC and PETRON shall carry on their operations and conduct their affairs in accordance with sound administrative, financial, engineering and industry practices under the supervision of qualified and experienced management assisted by competent staff in adequate numbers.

Section 3.02. PNOC-EDC and PETRON shall at all times operate and maintain their plant, machinery, equipment and other property, and from time to time, promptly as needed, make all necessary repairs and renewals thereof, all in accordance with sound engineering, financial and industry practices.

Section 3.03. PNOC-EDC and PETRON shall take out and maintain with responsible insurers, or make other provision satisfactory to the Bank for, insurance against such risks and in such amounts as shall be consistent with appropriate practice.

Section 3.04. PNOC-EDC and PETRON shall, by November 15 of each year, prepare its investment plan for the forthcoming year and for the following four years and furnish such plan to the Bank for its review and comment.

ARTICLE IV

Financial Covenants

Section 4.01. (a) PNOC-EDC and PETRON shall maintain records and accounts adequate to reflect in accordance with sound accounting practices their operations and financial condition.

(b) PNOC-EDC and PETRON shall:

- (i) have their records, accounts and financial statements (balance sheets, statements of income and expenses and related statements) for each fiscal year audited, in accordance with appropriate auditing principles consistently applied, by independent auditors acceptable to the Bank;
- (ii) furnish to the Bank as soon as available, but in any case not later than six months after the end of each such year, (A) certified copies of their financial

statements for such year as so audited, and (B) the report of such audit by said auditors of such scope and in such detail as the Bank shall have reasonably requested; and

- (iii) furnish to the Bank such other information concerning said records, accounts and financial statements as well as the audit thereof, as the Bank shall from time to time reasonably request.

Section 4.02. (a) Except as the Bank shall otherwise agree, PNOC-EDC and PETRON shall maintain a ratio of current assets to current liabilities of not less than 1 to 0.

(b) Before November 15 in each of its fiscal years, PNOC-EDC and PETRON shall, on the basis of forecasts prepared by PNOC-EDC and PETRON and satisfactory to the Bank, review whether it would meet the requirements set forth in paragraph (a) in respect of such year and the next following fiscal year and shall furnish to the Bank the results of such review upon its completion.

(c) If any such review shows that PNOC-EDC or PETRON would not meet the requirements set forth in paragraph (a) for PNOC-EDC's and PETRON's fiscal years covered by such review, PNOC-EDC and PETRON shall promptly take all necessary measures (including, without limitation, adjustments of the structure or levels of its rates) in order to meet such requirements.

(d) For the purposes of this Section:

- (i) The term "current assets" means cash, all assets which could in the ordinary course of business be converted into cash within twelve months, including accounts receivable, marketable securities, inventories and pre-paid expenses properly chargeable to operating expenses within the next fiscal year.
- (ii) The term "current liabilities" means all liabilities which will become due and payable or could under circumstances then existing be called for payment within twelve months, including accounts payable, customer advances, debt service requirements, taxes and payments in lieu of taxes, and dividends.
- (iii) The term "debt service requirements" means the aggregate amount of repayments (including sinking fund payments, if any) of, and interest and other charges on, debt.
- (iv) Whenever for the purposes of this Section it shall be necessary to value, in terms of the currency of the Guarantor, debt payable in another currency, such valuation shall be made on the basis of the prevailing lawful rate of exchange at which such other currency is, at the time

of such valuation, obtainable for the purposes of servicing such debt, or, in the absence of such rate, on the basis of a rate of exchange acceptable to the Bank.

Section 4.03. (a) Except as the Bank shall otherwise agree, PNOC-EDC and PETRON shall not incur any debt, if after the incurrence of such debt the ratio of debt to equity shall be greater than 70 to 30.

(b) For purposes of this Section:

- (i) The term "debt" means any indebtedness of PNOC-EDC and PETRON maturing by its terms more than one year after the date on which it is originally incurred and inter company advances classified as debt.
- (ii) Debt shall be deemed to be incurred: (A) under a loan contract or agreement or other instrument providing for such debt or for the modification of its terms of payment, on the date, and to the extent, the amount of such debt has become outstanding pursuant to such contract, agreement or instrument; and (B) under a guarantee agreement, on the date the agreement providing for such guarantee has been entered into but only to the extent that the guaranteed debt is outstanding.
- (iii) The term "equity" means the sum of the total unimpaired paid-up capital, retained earnings and reserves of PNOC-EDC and PETRON not allocated to cover specific liabilities.
- (iv) Whenever for the purposes of this Section it shall be necessary to value, in terms of the currency of the Guarantor, debt payable in another currency, such valuation shall be made on the basis of the prevailing lawful rate of exchange at which such other currency is, at the time of such valuation, obtainable for the purposes of servicing such debt, or, in the absence of such rate, on the basis of a rate of exchange acceptable to the Bank.

Section 4.04. (a) Except as the Bank shall otherwise agree, PNOC-EDC and PETRON shall not incur any debt unless a reasonable forecast of the revenues and expenditures of PNOC-EDC and PETRON shows that the estimated net revenues of PNOC-EDC and PETRON for each fiscal year during the term of the debt to be incurred shall be at least 1.2 times the estimated debt service requirements of PNOC - EDC or PETRON in such year on all debt of PNOC - EDC or PETRON including the debt to be incurred.

(b) For the purposes of this Section:

- (i) The term "debt" means any indebtedness of

PNOC-EDC or PETRON maturing by its terms more than one year after the date on which it is originally incurred excluding inter company advances classified as debt .

- (ii) Debt shall be deemed to be incurred: (A) under a loan contract or agreement or other instrument providing for such debt or for the modification of its terms of payment on the date of such contract, agreement or instrument; and (B) under a guarantee agreement, on the date the agreement providing for such guarantee has been entered into.
- (iii) The term "net revenues" means the difference between:
 - (A) the sum of revenues from all sources related to operations and net non-operating income; and
 - (B) the sum of all expenses related to operations including administration, adequate maintenance, taxes and payment in lieu of taxes, but excluding provision for depreciation, other non-cash operating charges and interest and other charges on debt.
- (iv) The term "net non-operating income" means the difference between:
 - (A) revenues from all sources other than those related to operations; and
 - (B) expenses, including taxes and payments in lieu of taxes, incurred in the generation of revenues in (A) above.
- (v) The term "debt service requirements" means the aggregate amount of repayments (including sinking fund payments, if any) of, and interest and other charges on, debt.
- (vi) The term "reasonable forecasts" means a forecast prepared by PNOC-EDC and PETRON not earlier than six months prior to the incurrence of the debt in question, which both the Bank and PNOC-EDC and PETRON accept as reasonable and as to which the Bank has notified PNOC-EDC and PETRON of its acceptability, provided that no event has occurred since such notification which has, or may reasonably be expected in the future to have, a material adverse effect on the financial condition or future operating results of PNOC-EDC and PETRON.
- (vii) Whenever for the purposes of this Section it shall be necessary to value, in terms of the currency of

By /s/ Emmanuel Pelaez
Authorized Representative

PETRON Corporation

By /s/ Emmanuel Pelaez
Authorized Representative

SCHEDULE 1

Procurement and Consultants' Services

Section I: Procurement of Goods and Works

Part A: International Competitive Bidding

Except as provided in Part C hereof, goods and works shall be procured under contracts awarded in accordance with procedures consistent with those set forth in Sections I and II of the "Guidelines for Procurement under IBRD Loans and IDA Credits" published by the Bank in May 1985 (the Guidelines).

Part B: Preference for Domestic Manufacturers

In the procurement of goods in accordance with the procedures described in Part A hereof, goods manufactured in the Republic of the Philippines may be granted a margin of preference in accordance with, and subject to, the provisions of paragraphs 2.55 and 2.56 of the Guidelines and paragraphs 1 through 4 of Appendix 2 thereto.

Part C: Other Procurement Procedures

Packages for equipment, materials and services may be procured under contracts awarded on the basis of either (a) local competitive bidding, advertised locally, in accordance with procedures satisfactory to the Bank said contracts shall not exceed \$200,000 per contract and up to an amount of \$2,000,000 in the aggregate, or (b) through limited international bidding procedures on the basis of evaluation and comparison of bids invited from a list of at least three qualified suppliers eligible under the Guidelines and in accordance with procedures set forth in Sections I and II of the Guidelines (excluding paragraphs 2.8, 2.9, 2.55 and 2.56 thereof), said contracts shall not exceed \$30,000,000 in the aggregate, or (c) on the basis of direct contracting for proprietary and trial equipment not exceeding an amount of \$5,000,000 in the aggregate.

Part D: Review by the Bank of Procurement Decisions

1. Review of invitations to bid and of proposed awards and final contracts:

(a) With respect to each contract estimated to cost the equivalent of \$1,000,000 or more, the procedures set forth in paragraphs 2 and 4 of Appendix 1 to the Guidelines shall apply. Where payments for such contract are to be made out of the Special Account, such

procedures shall be modified to ensure that the two conformed copies of the contract required to be furnished to the Bank pursuant to said paragraph 2 (d) shall be furnished to the Bank prior to the making of the first payment out of the Special Account in respect of such contract.

(b) With respect to each contract not governed by the preceding paragraph, the procedures set forth in paragraphs 3 and 4 of Appendix 1 to the Guidelines shall apply. Where payments for such contract are to be made out of the Special Account, such procedures shall be modified to ensure that the two conformed copies of the contract together with the other information required to be furnished to the Bank pursuant to said paragraph 3 shall be furnished to the Bank as part of the evidence to be furnished pursuant to paragraph 4 of Schedule 4 to the Loan Agreement.

2. The figure of 15% is hereby specified for purposes of paragraph 4 of Appendix I to the Guidelines.

Section II: Employment of Consultants

In order to assist PNOC-EDC and PETRON in carrying out Part A (1) and (2) of the Project, PNOC-EDC and PETRON shall employ consultants whose qualifications, experience and terms and conditions of employment shall be satisfactory to the Bank. Such consultants shall be selected in accordance with principles and procedures satisfactory to the Bank on the basis of the "Guidelines for the Use of Consultants by World Bank Borrowers and by the World Bank as Executing Agency" published by the Bank in August 1981.

SCHEDULE 2

Implementation Program

1. PNOC-EDC and PETRON shall, after completion of the delineation work at each geothermal site, prepare a resource assessment and development strategy study in a manner satisfactory to the Bank.

2. PNOC-EDC and PETRON shall, furnish annually to the Bank for its review and comments the drilling and development program for the coming year for the areas covered under Part A of the project.

