

CONFORMED COPY

LOAN NUMBER 4512 HU

Loan Agreement

(Municipal Wastewater Project)

between

INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT

and

MUNICIPALITY OF BUDAPEST

Dated September 22, 1999

LOAN NUMBER 4512 HU

LOAN AGREEMENT

AGREEMENT, dated September 22, 1999, between INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT (the Bank) and MUNICIPALITY OF BUDAPEST (the Borrower).

WHEREAS (A) Republic of Hungary (the Guarantor) and the Borrower, having been satisfied as to the feasibility and priority of the Project described in Schedule 2 to this Agreement, have requested the Bank to assist in the financing of the Project;

(B) by an agreement (the Guarantee Agreement) of even date herewith between the Guarantor and the Bank, the Guarantor has agreed to guarantee the obligations of the Borrower in respect of the Loan and to undertake such other obligations as set forth in the Guarantee Agreement;

(C) the Project will be carried out by the Borrower with the technical assistance of the Budapest Municipal Sewerage Company Ltd. (BMSC);

(D) the Guarantor has obtained from the European Community (EC) in the framework of the Large Scale Infrastructure Facility, a grant (the EC Grant) in the amount of EUR 16,000,000 to be made available to the Borrower for purposes of the Project under terms and conditions set forth in an agreement (the EC Financing Memorandum) dated December 23, 1998, between the Guarantor and the EC; and

(E) the Borrower has entered into the Public Utility Service Contract of November 3, 1997 with BMSC (the Contract) for the provision by BMSC of sewerage services and sewage treatment services, including technical supervision of construction of sewage treatment plants; and

WHEREAS the Bank has agreed, on the basis, inter alia, of the foregoing, to extend the Loan to the Borrower upon the terms and conditions set forth in this Agreement;

NOW THEREFORE the parties hereto hereby agree as follows:

ARTICLE I

General Conditions; Definitions

Section 1.01. The "General Conditions Applicable to Loan and Guarantee Agreements for Single Currency Loans" of the Bank, dated May 30, 1995 (as amended through December 2, 1997) (the General Conditions) constitute an integral part of this Agreement.

Section 1.02. Unless the context otherwise requires, the several terms defined in the General Conditions and in the Preamble to this Agreement have the respective meanings therein set forth and the following additional terms have the following meanings:

(a) "BMSC" means Budapest Municipal Sewerage Company, Ltd., a limited liability company established pursuant to Act No. LV of 1992 of the Guarantor based on the regulations established in Act No. LIV of 1992 of the Guarantor pursuant to Resolution No. 1317/1993 (XI.25.) of the General Assembly of the Municipality of Budapest and to the Deed of Foundation dated December 1, 1993, or any successor thereto;

(b) "Eligible Categories" means Categories (1), (2) and (3) set forth in the table in Part A.1 of Schedule 1 to this Agreement;

(c) "Eligible Expenditures" means the expenditures for works, goods and services referred to in Section 2.02 of this Agreement;

(d) "Euro" and "EUR" each means the lawful currency of the member states of the European Union that adopt the single currency in accordance with the Treaty establishing the European Community, as amended by the Treaty of the European Union;

(e) "fiscal year" means the period beginning January 1 and ending December 31;

(f) "PIU" means the project implementation unit established by the Borrower within the Mayor's Office of the Municipality of Budapest in September 1993;

(g) "Project Management Report" means each report prepared in accordance with Section 4.02 of this Agreement; and

(h) "Special Account" means the account referred to in Part B of Schedule 1 to this Agreement.

ARTICLE II

The Loan

Section 2.01. The Bank agrees to lend to the Borrower, on the terms and conditions set forth or referred to in the Loan Agreement, an amount equal to twenty seven million six hundred thousand Euro (EUR 27,600,000).

Section 2.02. The amount of the Loan may be withdrawn from the Loan Account in accordance with the provisions of Schedule 1 to this Agreement for expenditures made (or, if the Bank shall so agree, to be made) in respect of the reasonable cost of goods, works and services required for the Project described in Schedule 2 to this

Agreement and to be financed out of the proceeds of the Loan.

Section 2.03. The Closing Date shall be December 31, 2006, or such later date as the Bank shall establish. The Bank shall promptly notify the Borrower and the Guarantor of such later date.

Section 2.04. The Borrower shall pay to the Bank a fee in an amount equal to one percent (1%) of the amount of the Loan. On or promptly after the Effective Date, the Bank shall, on behalf of the Borrower, withdraw from the Loan Account and pay to itself the amount of said fee.

Section 2.05. The Borrower shall pay to the Bank a commitment charge at the rate of three-fourths of one percent (3/4 of 1%) per annum on the principal amount of the Loan not withdrawn from time to time.

Section 2.06. (a) The Borrower shall pay interest on the principal amount of the Loan withdrawn and outstanding from time to time, at a rate for each Interest Period equal to LIBOR Base Rate plus LIBOR Total Spread.

(b) For the purposes of this Section:

(i) "Interest Period" means the initial period from and including the date of this Agreement to, but excluding, the first Interest Payment Date occurring thereafter, and after the initial period, each period from and including an Interest Payment Date to, but excluding the next following Interest Payment Date.

(ii) "Interest Payment Date" means any date specified in Section 2.07 of this Agreement.

(iii) "LIBOR Base Rate" means, for each Interest Period, the London interbank offered rate for six-month deposits in Euro for value the first day of such Interest Period (or, in the case of the initial Interest Period, for value the Interest Payment Date occurring on or next preceding the first day of such Interest Period), as reasonably determined by the Bank and expressed as a percentage per annum.

(iv) "LIBOR Total Spread" means, for each Interest Period: (A) three-fourths of one percent (3/4 of 1%); (B) minus (or plus) the weighted average margin, for such Interest Period, below (or above) the London interbank offered rates, or other reference rates, for six-month deposits, in respect of the Bank's outstanding borrowings or portions thereof allocated by the Bank to fund single currency loans or portions thereof made by it that include the Loan, as reasonably determined by the Bank and expressed as a percentage per annum.

(c) The Bank shall notify the Borrower and Guarantor of LIBOR Base Rate and LIBOR Total Spread for each Interest Period, promptly upon the determination thereof.

(d) Whenever, in light of changes in market practice affecting the determination of the interest rates referred to in this Section 2.06, the Bank determines that it is in the interest of its borrowers as a whole and of the Bank to apply a basis for determining the interest rates applicable to the Loan other than as provided in said Section, the Bank may modify the basis for determining the interest rates applicable to the Loan upon not less than six (6) months' notice to the Borrower and the Guarantor of the new basis. The new basis shall become effective on the expiry of the notice period unless the Borrower or the Guarantor notifies the Bank during said period of its objection thereto, in which case said modification shall not apply to the Loan.

Section 2.07. Interest and other charges shall be payable April 15 and October 15 in each year.

Section 2.08. The Borrower shall repay the principal amount of the Loan in accordance with the amortization schedule set forth in Schedule 3 to this Agreement.

ARTICLE III

Execution of the Project

Section 3.01. (a) The Borrower declares its commitment to the objectives of the Project as set forth in Schedule 2 to this Agreement, and, to this end, shall carry out the Project through the PIU with the technical assistance of BMSC with due diligence and efficiency and in conformity with appropriate administrative, financial, engineering, public utility and environmental practices and shall provide, 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 Borrower and the Bank shall otherwise agree, the Borrower shall maintain the PIU until the completion of the Project, and ensure that the PIU functions at all times in accordance with operating procedures and with staff and budgetary resources necessary to meet the objectives of the Project.

Section 3.02. The Borrower shall carry out the Project in accordance with an environmental management plan agreed upon with the Bank.

Section 3.03. Except as the Bank shall otherwise agree, procurement of the goods, works and consultants' services required for the Project and to be financed out of the proceeds of the Loan shall be governed by the provisions of Schedule 4 to this Agreement.

Section 3.04. For the purposes of Section 9.08 of the General Conditions and without limitation thereto, the Borrower shall:

(a) prepare, on the basis of guidelines acceptable to the Bank, and furnish to the Bank not later than six (6) months after the Closing Date or such later date as may be agreed for this purpose between the Borrower and the Bank, a plan for the future operation of the Project; and

(b) afford the Bank a reasonable opportunity to exchange views with the Borrower on said plan.

Section 3.05. (a) The Borrower shall maintain policies and procedures adequate to enable it to monitor and evaluate on an ongoing basis, in accordance with indicators acceptable to the Bank, the carrying out of the Project and the achievement of the objectives thereof;

(b) prepare, under terms of reference satisfactory to the Bank, and furnish to the Bank, on or about December 31, 2002, a report integrating the results of the monitoring and evaluation activities performed pursuant to paragraph (a) of this Section, on the progress achieved in the carrying out of the Project during the period preceding the date of said report and setting out the measures recommended to ensure the efficient carrying out of the Project and the achievement of the objectives thereof during the period following such date; and

(c) review with the Bank, by March 31, 2003, or such later date as the Bank shall request, the report referred to in paragraph (b) of this Section, and, thereafter, take all measures required to ensure the efficient completion of the Project and the achievement of the objectives thereof, based on the conclusions and recommendations of the said report and taking into consideration the Bank's views on the matter.

ARTICLE IV

Financial Covenants

Section 4.01. (a) The Borrower shall establish and maintain a financial management system, including records and accounts, and prepare financial statements, all in accordance with accounting standards acceptable to the Bank, consistently applied, adequate to reflect its operations and financial condition and to register separately the operations, resources and expenditures for and in connection with the carrying out of the Project.

(b) The Borrower shall:

(i) have its records, accounts and financial statements (balance sheets, statements of income and expenses and related statements) for each fiscal year audited, in accordance with auditing standards acceptable to the Bank, 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 the financial statements referred to in paragraph (a) of this Section, for such year as so audited; and (B) an opinion on such statements and 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 such records, accounts, and financial statements, and the audit thereof, as the Bank may from time to time reasonably request.

(c) For all expenditures with respect to which withdrawals from the Loan Account were made on the basis of Project Management Reports or statements of expenditures the Borrower shall:

(i) maintain or cause to be maintained, in accordance with paragraph (a) of this Section, records and separate accounts reflecting expenditures related to the Project.

(ii) retain, until at least one year after the Bank has received the audit report for the fiscal year in which the last withdrawal from the Loan Account was made, all records and related supporting documents (contracts, orders, invoices, bills, receipts and other documents) evidencing such expenditures;

(iii) enable the Bank's representatives to examine such records; and

(iv) ensure that such records and accounts are included in the annual audit referred to in paragraph (b) of this Section and that the report of such audit contains a separate opinion by said auditors as to whether the statements of expenditure or Project Management Reports submitted during such fiscal year, together with the procedures and internal controls involved in their preparation, can be relied upon to support the related withdrawals.

Section 4.02. (a) Without limitation upon the provisions of Section 4.01 of this Agreement, the Borrower shall carry out a time-bound action plan acceptable to the Bank for the strengthening of the financial management system referred to in paragraph (a) of said Section 4.01 in order to enable the Borrower, not later than December 31, 1999, or such later date as the Bank shall agree, to prepare quarterly Project Management Reports, acceptable to the Bank, each of which:

(i) (A) sets forth actual sources and applications of funds for the Project, both cumulatively and for the period covered by said report, and projected sources and applications of funds for the Project for the six-month period following the period covered by said report; and (B) shows separately expenditures financed out of the proceeds of the Loan during the period covered by said report and expenditures proposed to be financed out of the proceeds of the Loan during the six-month period following the period covered by said report;

(ii) (A) describes physical progress in Project implementation, both cumulatively and for the period covered by said report, and (B) explains variances between the actual and previously forecast implementation targets; and

(iii) sets forth the status of procurement under the Project and expenditures under contracts financed out of the proceeds of the Loan,

as at the end of the period covered by said report.

(b) Upon the completion of the action plan referred to in paragraph (a) of this Section, the Borrower shall prepare, in accordance with guidelines acceptable to the Bank, and furnish to the Bank not later than 45 days after the end of each calendar quarter a Project Management Report for such period.

Section 4.03 (a) The Borrower shall, to the extent it has legal power, cause BMSC to maintain records and accounts adequate to reflect in accordance with sound accounting practices its operations and financial condition.

(b) The Borrower shall, to the extent it has legal power, cause BMSC to:

(i) have the 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, internationally recognized auditors;

(ii) furnish to the Bank through the Borrower as soon as available, but in any case not later than six (6) months after the end of each such year: (A) certified copies of its financial statements for such year 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 through the Borrower under a confidentiality agreement such other information concerning such records, accounts and financial statements and the audit thereof as the Bank shall from time to time reasonably request.

Section 4.04. (a) Except as the Bank shall otherwise agree, the Borrower shall not incur any debt, if in the period succeeding the incurrence of such debt, the ratio of the Borrower's projected operating surplus to the Borrower's debt service obligations would fall below 1.5 for one of any two successive fiscal years or below 1.1 for any given fiscal year.

(b) For the purpose of this Section:

(i) the term "debt" means any indebtedness of the Borrower maturing by its terms more than one year after the date on which it is originally incurred.

(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, but only to the extent that the guaranteed debt shall be outstanding.

(iii) the term "projected operating surplus" means the excess of the Borrower's projected total current revenues from all sources, including transfers from the Guarantor, excluding any borrowings, and the Borrower's projected total current expenditures, excluding those for debt service obligations; and

(iv) the term "debt service obligations" means the total of interest and other financial charges, and the repayment of principal, on all medium and long term liabilities of the Borrower, including, but not limited to, loans and bonds.

Section 4.05. The Borrower shall use its revenues derived from the provision of wastewater, flood control and drainage services (development fund, leasing fees related to wastewater services and dividends) only for financing operations, investments and debt service related thereto.

Section 4.06. The Borrower shall:

(a) take all measures necessary, including the adjustment of tariffs, to: (i) provide, in a timely manner each year, the Borrower's share of the financing for the Project; and (ii) permit BMSC to maintain sound financial and operating conditions as required under the Contract;

(b) not later than January 31 of each year, exchange views with the Bank on the tariffs established for that year, together with information showing the basis for establishing said tariffs, and forecasts showing the adequacy of the tariffs to meet the objectives specified under paragraph (a) above; and

(c) in the event that it is determined during said exchange of views that shortfalls in funds are likely to occur such as to prevent the achievement of said objectives, promptly to take, or, to the extent legally and practically possible, cause BMSC to take remedial action to cover the shortfalls.

Section 4.07. The Borrower shall:

(a) not later than June 30, 2001, carry out the study referred to in Part E.2 of the Project;

(b) not later than September 30, 2001, jointly review with the Bank the findings and recommendations of such study; and

(c) by January 1, 2003, implement the recommendations of such study, taking into consideration the Bank's comments on such recommendations.

ARTICLE V

Other Covenants

Section 5.01. The Borrower shall, to the extent it has the legal power and it is practically feasible, cause BMSC to:

(a) carry on its operations and conduct its affairs in accordance with sound administrative, financial, engineering, public utility and environmental practices under the supervision of qualified and experienced management assisted by competent staff in adequate numbers;

(b) at all times operate and maintain its plants, 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 public utility practices; and

(c) 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 public utility practices.

Section 5.02. The Borrower shall promptly notify the Bank of the proposed modification of any material provision of the Contract and, in the event of a material modification affecting the provision of wastewater services or the termination of the Contract, the Borrower shall consult with the Bank as to the alternative arrangements to be adopted for the provision of wastewater services.

ARTICLE VI

Remedies of the Bank

Section 6.01. Pursuant to Section 6.02 (p) of the General Conditions, the following additional events are specified:

(a) (i) Subject to subparagraph (ii) of this paragraph, the right of the Guarantor to withdraw the proceeds of the EC Grant for purposes of the Project shall have been suspended, canceled or terminated in whole or in part, pursuant to the terms of the Financing Memorandum providing therefor.

(ii) Subparagraph (i) of this paragraph shall not apply if the Borrower establishes to the satisfaction of the Bank that: (A) such suspension, cancellation or termination is not caused by the failure of the Guarantor to perform any of its obligations under the Financing Memorandum; and (B) adequate funds for the Project are available to the Borrower from other sources on terms and conditions consistent with the obligations of the Borrower under this Agreement.

(b) The Contract shall have been materially amended, suspended, abrogated or repealed without the prior consent of the Bank; which consent shall not unreasonably be withheld.

Section 6.02 Pursuant to Section 7.01 (k) of the General Conditions, the following additional events are specified:

(a) the event specified in paragraph (a) (i) of Section 6.01 of this Agreement shall occur, subject to the proviso of paragraph (a) (ii) of that Section; and

(b) the event specified in paragraph (b) of Section 6.01 of this Agreement shall occur and shall continue for a period of ninety days after notice thereof shall have been given by the Bank to the Borrower.

ARTICLE VII

Termination

Section 7.01. The date ninety (90) days after the date of this Agreement is hereby specified for the purposes of Section 12.04 of the General Conditions.

ARTICLE VIII

Representative of the Borrower; Addresses

Section 8.01. The Mayor of the Municipality of Budapest is designated as representative of the Borrower for the purposes of Section 11.03 of the General Conditions.

Section 8.02. The following addresses are specified for the purposes of Section 11.01 of the General Conditions:

For the Borrower:

Municipality of Budapest
Mayor's Office
P.O. Box 1
H-1364 Budapest 4
Republic of Hungary

Cable address:

MUNICIPALITY OF
BUDAPEST

Fax:

36 1 3271811

For the Bank:

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

Cable address:

INTBAFRAD

Telex:

248423 (MCI) or

Washington, D.C.

64145 (MCI)

IN WITNESS WHEREOF, the parties hereto, acting through their duly authorized representatives, have caused this Agreement to be signed in their respective names in Budapest, Republic of Hungary, as of the day and year first above written.

INTERNATIONAL BANK FOR
RECONSTRUCTION AND DEVELOPMENT

By /s/ Roger Grawe

Authorized Representative

MUNICIPALITY OF BUDAPEST

By /s/ Gabor Demszky

Authorized Representative

SCHEDULE 1

Withdrawal of the Proceeds of the Loan

A. General

1. The table below sets forth the Categories of items to be financed out of the proceeds of the Loan, the allocation of the amounts of the Loan to each Category and the percentage of expenditures for items so to be financed in each Category:

Category	Amount of the Loan (Expressed in EUR)	% of Expenditures to be Financed
(1) Works (except for Parts A.1 and C.1 of the Project)	20,600,000	50%
(2) Goods (except for Parts A.1 and C.1 of the Project)	3,520,000	50%
(3) Consultants' services	470,000	100%
(4) Fee	276,000	Amount due under Section 2.04 of this Agreement
(5) Unallocated	2,734,000	
TOTAL	27,600,000	

2. Notwithstanding the provisions of paragraph 1 above, no withdrawals shall be made in respect of: (a) payments made for expenditures prior to the date of this Agreement, except that withdrawals, in an amount not exceeding the equivalent of EUR 9,300,000, may be made in respect of Categories (1), (2) and (3) set forth in the table in paragraph 1 of this Schedule on account of payments made for expenditures before that date but after January 1, 1998.

3. The Bank may require withdrawals from the Loan Account to be made on the basis

of statements of expenditure for expenditures for services under contracts costing less than \$100,000 equivalent each, under such terms and conditions as the Bank shall specify by notice to the Borrower.

B. Special Account

1. The Borrower shall open and maintain a special deposit account in EUR in a commercial bank, acceptable to the Bank, on terms and conditions satisfactory to the Bank, including appropriate protection against set-off, seizure and attachment.

2. After the Bank has received evidence satisfactory to it that the Special Account has been opened, withdrawals from the Loan Account of amounts to be deposited into the Special Account shall be made as follows:

(a) until the Bank shall have received: (i) the first Project Management Report referred to in Section 4.02(b) of this Agreement; and (ii) a request from the Borrower for withdrawal on the basis of Project Management Reports, withdrawals shall be made in accordance with the provisions of Annex A to this Schedule 1; and

(b) upon receipt by the Bank of a Project Management Report pursuant to Section 4.02(b) of this Agreement, accompanied by a request from the Borrower for withdrawal on the basis of Project Management Reports, all further withdrawals shall be made in accordance with the provisions of Annex B to this Schedule 1.

3. Payments out of the Special Account shall be made exclusively for eligible expenditures. For each payment made by the Borrower out of the Special Account, the Borrower shall, at such time as the Bank shall reasonably request, furnish to the Bank such documents and other evidence showing that such payment was made exclusively for Eligible Expenditures.

4. Notwithstanding the provisions of Part B.2 of this Schedule, the Bank shall not be required to make further deposits into the Special Account:

(a) if the Bank determines at any time that any Project Management Report does not adequately provide the information required pursuant to Section 4.02 of this Agreement;

(b) if the Bank determines at any time that all further withdrawals should be made by the Borrower directly from the Loan Account; or

(c) if the Borrower shall have failed to furnish to the Bank within the period of time specified in Section 4.01(b)(ii) of this Agreement, any of the audit reports required to be furnished to the Bank pursuant to said Section in respect of the audit of (A) the records and accounts for the Special Account; or (B) the records and accounts reflecting expenditures with respect to which withdrawals were made on the basis of Project Management Reports.

5. The Bank shall not be required to make further deposits into the Special Account in accordance with the provisions of Part B.2 of this Schedule if, at any time, the Bank shall have notified the Borrower of its intention to suspend in whole or in part the right of the Borrower to make withdrawals from the Loan Account pursuant to Section 6.02 of the General Conditions. Upon such notification, the Bank shall determine, in its sole discretion, whether further deposits into the Special Account may be made and what procedures should be followed for making such deposits, and shall notify the Borrower of its determination.

6. (a) If the Bank determines at any time that any payment out of the Special Account was made for an expenditure which is not an Eligible Expenditure, or was not justified by the evidence furnished to the Bank, the Borrower shall, promptly upon notice from the Bank, provide such additional evidence as the Bank may reasonably request, or deposit into the Special Account (or, if the Bank shall so request, refund to the Bank) an amount equal to the amount of such payment. Unless the Bank shall otherwise agree, no further deposit by the Bank into the Special Account shall be made until the Borrower has provided such evidence or made such deposit or refund, as the case may be.

(b) If the Bank determines at any time that any amount outstanding in the

Special Account will not be required to cover payments for Eligible Expenditures during the six-month period following such determination, the Borrower shall, promptly upon notice from the Bank, refund to the Bank such outstanding amount.

(c) The Borrower may, upon notice to the Bank, refund to the Bank all or any portion of the funds on deposit in the Special Account.

(d) Refunds to the Bank made pursuant to sub-paragraphs (a), (b) or (c) of this paragraph 6 shall be credited to the Loan Account for subsequent withdrawal or for cancellation in accordance with the provisions of the Loan Agreement.

ANNEX A TO SCHEDULE 1

Operation of Special Account When Withdrawals Are Not Made On the Basis of Project Management Reports

1. For the purposes of this Annex:

(a) the term "Authorized Allocations" means the equivalent of \$2,000,000 to be withdrawn from the Loan Account and deposited into the Special Account pursuant to paragraph 2 of this Annex; provided, however, that unless the Bank shall otherwise agree, the Authorized Allocation shall be limited to the equivalent of \$1,000,000 until the aggregate amount of withdrawals, plus the total amount of all outstanding special commitments entered into by the Bank pursuant to Section 5.02 of the General Conditions, shall equal or exceed the equivalent of \$3,000,000.

2. Withdrawals of the Authorized Allocations and subsequent withdrawals to replenish the Special Account shall be made as follows:

(a) For withdrawals of the Authorized Allocation, the Borrower shall furnish to the Bank a request or requests for deposit into the Special Account of an amount or amounts which in the aggregate do not exceed the Authorized Allocation for said Special Account. On the basis of each such request, the Bank shall, on behalf of the Borrower, withdraw from the Loan Account and deposit into the Special Account such amount as the Borrower shall have requested.

(b) For replenishment of the Special Account, the Borrower shall furnish to the Bank requests for deposit into the Special Account at such intervals as the Bank shall specify. Prior to or at the time of each such request, the Borrower shall furnish to the Bank the documents and other evidence required pursuant to Part B.3 of Schedule 1 to this Agreement for the payment or payments in respect of which replenishment is requested. On the basis of each such request, the Bank shall, on behalf of the Borrower, withdraw from the Loan Account and deposit into the Special Account, such amount as the Borrower shall have requested and as shall have been shown by said documents and other evidence to have been paid out of the Special Account for Eligible Expenditures. Each such deposit into the Special Account shall be withdrawn by the Bank from the Loan Account under one or more of the Eligible Categories.

3. The Bank shall not be required to make further deposits into the Special Account, once the total unwithdrawn amount of the Loan minus the total amount of all outstanding special commitments entered into by the Bank pursuant to Section 5.02 of the General Conditions, shall equal the equivalent of twice the amount of the Authorized Allocation. Thereafter, withdrawal from the Loan Account of the remaining unwithdrawn amount of the Loan shall follow such procedures as the Bank shall specify by notice to the Borrower. Such further withdrawals shall be made only after and to the extent that the Bank shall have been satisfied that all such amounts remaining on deposit in the Special Account as of the date of such notice will be utilized in making payments for Eligible Expenditures.

ANNEX B TO SCHEDULE 1

Operation of Special Account When Withdrawals Are Made On the Basis of Project Management Reports

1. Except as the Bank may otherwise specify by notice to the Borrower, all withdrawals from the Loan Account shall be deposited by the Bank into the Special Account in accordance with the provisions of Schedule 1 to this Agreement. Each such

deposit into the Special Account shall be withdrawn by the Bank from Loan Account under one or more of the Special Account's Eligible Categories.

2. Each application for withdrawal from the Loan Account for deposit into the Special Account shall be supported by a Project Management Report.

3. Upon receipt of each application for withdrawal of an amount of the Loan, the Bank shall, on behalf of the Borrower, withdraw from the Loan Account and deposit into the Special Account an amount equal to the lesser of: (a) the amount so requested; and (b) the amount which the Bank has determined, based on the Project Management Report accompanying said application, is required to be deposited in order to finance Eligible Expenditures during the six-month period following the date of such report; provided, however, that the amount so deposited, when added to the amount indicated by said Project Management Report to be remaining in the Special Account, shall not exceed the equivalent of \$5,000,000.

SCHEDULE 2

Description of the Project

The objectives of the Project are to: (i) reduce the pollution load in the Danube River Basin; (ii) strengthen compliance with Hungarian and European Union environmental standards; and (iii) improve wastewater operations in the water and wastewater utilities of the Borrower..

The Project consists of the following parts, subject to such modifications thereof as the Borrower and the Bank may agree upon from time to time to achieve such objectives:

Part A: North Budapest Wastewater Treatment Plant

1. Upgrading plant capacity from 140,000 m³/day to an average of 155,000 m³/day and a peak capacity of 200,000 m³/day, while maintaining eighty percent (80%) removal of chemical oxygen demand and suspended solids with provision for the removal of nitrogen and phosphorus in the future.
2. Upgrading of solids handling facilities.

Part B: South Pest Wastewater Treatment Plant

1. Upgrading and extending plant capacity from 72,000 m³/day to 80,000 m³/day, with the addition of nitrogen and phosphorus removal capability and provision for expansion in the future to 120,000 m³/day.
2. Upgrading and expansion of solids handling facilities.

Part C: North Buda Wastewater and Rainwater Pumping and Collection System

1. Construction of the Pok Street Pump Station with a capacity of 7,000 lps.
2. Construction of the Danube River siphon at Pok Street.
3. Construction of the North Buda Wastewater and Rainwater Collector system comprising 4,500 m of gravity trunk sewer and 1,800 m of pressure main.

Part D: Wastewater Monitoring System

Installation of a monitoring system for measuring and sampling of flows in the central wastewater collection network.

Part E: Technical Assistance

1. Carrying out of a study to recommend regulatory and technical measures to strengthen monitoring of industrial wastes discharged into the sewer system and to enforce standards related thereto.
2. Carry out of a study of the technical, financial and legal aspects of industrial

wastewater tariffs charged by BMSC to users of the wastewater system with the objective of implementing charges based on contaminants as well as quantity.

3. Completion of a study to determine the source of uncommon odors at the North Budapest Wastewater Treatment Plant and to recommend corrective measures.

* * *

The Project is expected to be completed by June 30, 2006.

SCHEDULE 3

Amortization Schedule

Date Payment Due	Payment of Principal (Expressed in EUR)*
On each April 15 and October 15 beginning April 15, 2005 through October 15, 2014	1,380,000

* The figures in this column represent the amount in EUR to be repaid, except as provided in Section 4.04 (d) of the General Conditions.

SCHEDULE 4

Procurement and Consultants' Services

Section I. Procurement of Goods and Works

Part A: General

Goods and works shall be procured in accordance with the provisions of Section I of the "Guidelines for Procurement under IBRD Loans and IDA Credits" published by the Bank in January 1995 and revised in January and August 1996, September 1997 and January 1999 (the Guidelines) and the following provisions of this Section, as applicable.

Part B: International Competitive Bidding

1. Goods and works shall be procured under contracts awarded in accordance with the provisions of Section II of the Guidelines and paragraph 5 of Appendix 1 thereto.

2. The following provisions shall apply to goods and works to be procured under

contracts awarded in accordance with the provisions of paragraph 1 of this Part B.

(a) Preference for Domestically Manufactured Goods

The provisions of paragraphs 2.54 and 2.55 of the Guidelines and Appendix 2 thereto shall apply to goods manufactured in the territory of the Guarantor.

(b) Notification and Advertising

The invitation to prequalify or bid for each contract estimated to cost \$10,000,000 equivalent or more shall be advertised in accordance with the procedures applicable to large contracts under paragraph 2.8 of the Guidelines.

Part C: Other Procurement Procedures

Goods estimated to cost less than \$400,000 equivalent per contract up to an aggregate amount not to exceed \$400,000 equivalent, may be procured under contracts awarded on the basis of international shopping procedures in accordance with the provisions of paragraphs 3.5 and 3.6 of the Guidelines.

Part D: Review by the Bank of Procurement Decisions

1. Procurement Planning

Prior to the issuance of any invitations to prequalify for bidding or to bid for contracts, the proposed procurement plan for the Project shall be furnished to the Bank for its review and approval, in accordance with the provisions of paragraph 1 of Appendix 1 to the Guidelines. Procurement of all goods and works shall be undertaken in accordance with such procurement plan as shall have been approved by the Bank, and with the provisions of said paragraph 1.

2. Prior Review

With respect to each contract other than contracts to be procured under the procedures referred to in Part C above, the procedures set forth in paragraphs 2 and 3 of Appendix 1 to the Guidelines shall apply.

3. Post Review

With respect to each contract not governed by paragraph 2 of this Part, the procedures set forth in paragraph 4 of Appendix 1 to the Guidelines shall apply.

Section II. Employment of Consultants

Part A: General

Consultants' services shall be procured in accordance with the provisions of the Introduction and Section IV of the "Guidelines: Selection and Employment of Consultants by World Bank Borrowers" published by the Bank in January 1997 and revised in September 1997 and January 1999 (the Consultant Guidelines) and the following provisions of Section II of this Schedule.

Part B: Quality- and Cost-based Selection

Except as otherwise provided in Part C of this Section, consultants' services shall be procured under contracts awarded in accordance with the provisions of Section II of the Consultant Guidelines, paragraph 3 of Appendix 1 thereto, and the provisions of paragraphs 3.13 through 3.18 thereof applicable to quality- and cost-based selection of consultants.

Part C: Other Procedures for the Selection of Consultants

Selection Based on Consultants' Qualifications Services for carrying out the Project estimated to cost less than \$100,000 equivalent per contract may be procured under contracts awarded in accordance with the provisions of paragraphs 3.1 and 3.7 of the Consultant Guidelines.

Part D: Review by the Bank of the Selection of Consultants

1. Selection Planning

Prior to issuance to consultants of any requests for proposals, the proposed plan for the selection of consultants under the Project shall be furnished to the Bank for its review and approval, in accordance with the provisions of paragraph 1 of Appendix 1 to the Consultant Guidelines. Selection of all consultants' services shall be undertaken in accordance with such selection plan as shall have been approved by the Bank, and with the provisions of said paragraph.

2. Prior Review

With respect to each contract for the employment of consulting firms estimated to cost the equivalent of \$100,000 or more, the procedures set forth in paragraphs 1, 2 (other than the third subparagraph of paragraph 2(a)) and 5 of Appendix 1 to the Consultant Guidelines shall apply.

3. Post Review

With respect to each contract not governed by paragraph 1 of this Part, the procedures set forth in paragraph 4 of Appendix 1 to the Consultant Guidelines shall apply.

