

CONFORMED COPY

LOAN NUMBER 3264 HU

(Second Telecommunications Project)

between

INTERNATIONAL BANK FOR RECONSTRUCTION
AND DEVELOPMENT

and

HUNGARIAN TELECOMMUNICATIONS COMPANY

Dated October 29, 1990

LOAN NUMBER 3264 HU

LOAN AGREEMENT

AGREEMENT, dated October 29, 1990, between INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT (the Bank) and HUNGARIAN TELECOMMUNICATIONS COMPANY (the Borrower).

WHEREAS (A) the 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; 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" of the Bank, dated January 1, 1985, with the last sentence of Section 3.02 deleted (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) "Establishment Resolution" means Resolution No. 965, 292/1989, dated December 20, 1989, of the Guarantor's Minister of Transport, Communications and Construction, pertaining to the establishment and operations of the Borrower;

(b) "Action Plan" means the Borrower's plan of actions for the further development of its organization, management, operations and financial condition over the 1991-1993 period and whose outline is set forth in Schedule 6 to this Agreement;

(c) "Project Unit" means the Project unit established by the Borrower and to be maintained in accordance with the provisions of Section 3.01 (b) of this Agreement; and

(d) "Special Account" means the account referred to in Section 2.02 (b) of 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 this Agreement, various currencies that shall have an aggregate value equivalent to the amount of one hundred fifty million dollars (\$150,000,000), being the sum of withdrawals of the proceeds of the Loan, with each withdrawal valued by the Bank as of the date of such withdrawal.

Section 2.02. (a) 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 and services required for the Project and to be financed out of the proceeds of the Loan.

(b) The Borrower shall, for the purposes of the Project, open and maintain in dollars a special deposit account in National Bank of Hungary on terms and conditions satisfactory to the Bank. Deposits into, and payments out of, the Special Account shall be made in accordance with the provisions of Schedule 5 to this Agreement.

Section 2.03. The Closing Date shall be June 30, 1996, 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 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 2.05. (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 the Cost of Qualified Borrowings determined in respect of the preceding Semester, plus one-half of one percent ($1/2$ of 1%). On each of the dates specified in Section 2.06 of this Agreement, the Borrower shall pay interest accrued on the principal amount outstanding

during the preceding Interest Period, calculated at the rate applicable during such Interest Period.

(b) As soon as practicable after the end of each Semester, the Bank shall notify the Borrower and the Guarantor of the Cost of Qualified Borrowings determined in respect of such Semester.

(c) For the purposes of this Section:

- (i) "Interest Period" means a six-month period ending on the date immediately preceding each date specified in Section 2.06 of this Agreement, beginning with the Interest Period in which this Agreement is signed.
- (ii) "Cost of Qualified Borrowings" means the cost, as reasonably determined by the Bank and expressed as a percentage per annum, of the outstanding borrowings of the Bank drawn down after June 30, 1982, excluding such borrowings or portions thereof as the Bank has allocated to fund: (A) the Bank's investments; and (B) loans which may be made by the Bank after July 1, 1989, bearing interest rates determined otherwise than as provided in paragraph (a) of this Section.
- (iii) "Semester" means the first six months or the second six months of a calendar year.

(d) On such date as the Bank may specify by no less than six months' notice to the Borrower, paragraphs (a), (b) and (c) (iii) of this Section shall be amended to read as follows:

"(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 Quarter equal to the Cost of Qualified Borrowings determined in respect of the preceding Quarter, plus one-half of one percent (1/2 of 1%). On each of the dates specified in Section 2.06 of this Agreement, the Borrower shall pay interest accrued on the principal amount outstanding during the preceding Interest Period, calculated at the rates applicable during such Interest Period."

"(b) As soon as practicable after the end of each Quarter, the Bank shall notify the Borrower and the Guarantor of the Cost of Qualified Borrowings determined in respect of such Quarter."

"(c) (iii) 'Quarter' means a three-month period commencing on January 1, April 1, July 1 or October 1 in a calendar year."

Section 2.06. Interest and other charges shall be payable semiannually on May 15 and November 15 in each year.

Section 2.07. The Borrower shall repay the principal amount of the Loan in accordance with the amortization schedule set forth in Schedule 3 to this Agreement.

Section 2.08. The President of the National Bank of Hungary, or such other person or persons as said President shall designate in writing, are designated as representatives of the Borrower for the purposes of taking any action required or permitted to be taken under the provisions of Section 2.02 of this Agreement and Article V of the General Conditions.

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 with due diligence and efficiency and in conformity with appropriate administrative, financial, engineering and telecommunications practices, and shall provide, promptly as needed, the funds, facilities, services and other resources required for the Project.

(b) In order to facilitate the efficient carrying out of the Project, the Borrower shall: (i) maintain the Project Unit with resources and terms of reference satisfactory to the Bank, to coordinate, supervise and report on project execution and the procurement of goods and services therefor; and (ii) employ, as needed, consultants with qualifications and experience and under terms of reference satisfactory to the Bank, to assist in the carrying out of the Project.

Section 3.02. Except as the Bank shall otherwise agree, procurement of the goods 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.

ARTICLE IV

Management and Operations of the Borrower

Section 4.01. (a) The Borrower shall: (i) carry on its operations and conduct its affairs in accordance with sound administrative, financial, engineering and telecommunications practices under the supervision of qualified and experienced management assisted by competent staff in adequate number; (ii) at all times take all steps required to maintain and renew all rights, powers, privileges and franchises necessary or useful in the conduct of its business; and (iii) by July 1, 1991, reconstitute itself as a joint-stock company under the laws of the Guarantor.

(b) Without limitation on the generality of paragraph (a) of this Section, the Borrower shall:

- (i) carry out the Action Plan with due diligence and efficiency and all times take all necessary action to achieve the objectives thereof;
- (ii) maintain policies and procedures adequate to enable it to monitor and evaluate, in accordance with indicators satisfactory to the Bank, the carrying out of the Action Plan and the achievement of the objectives thereof;
- (iii) prepare and furnish to the Bank for review and comments, by May 31 and November 30 of each year, progress reports, in form and substance satisfactory to the Bank, on the progress achieved in the carrying out of the Action Plan and the measures recommended to sustain and further such progress based on the results of the monitoring and evaluation activities performed pursuant to subparagraph (ii) of this paragraph; and
- (iv) by June 30 of each year, update the Action Plan and thereafter implement the measures required to ensure the achievement of the objectives thereof, taking into consideration the conclusions and recommendations of the progress reports prepared pursuant to subparagraph (iii) of this paragraph and the Bank's comments thereon.

Section 4.02. The Borrower shall:

(a) furnish to the Bank, for its review and comments, a copy of each of the studies provided under Part B (2) of the Project upon

its completion; and

(b) thereafter, develop and carry out, on the basis of a schedule satisfactory to the Bank, a plan of action to achieve the objectives of such study, taking into consideration the recommendations thereof and the Bank's comments thereon.

Section 4.03. The Borrower shall at all times operate and maintain its plant, facilities, machinery, equipment, installations 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 telecommunications practices.

Section 4.04. The Borrower 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.

ARTICLE V

Financial Covenants

Section 5.01. (a) The Borrower shall maintain records and accounts adequate to reflect in accordance with sound accounting practices its operations and financial condition.

(b) The Borrower shall:

- (i) have its records, accounts and financial statements (balance sheets, statements of income and expenses and related statements) and the records and accounts for the Special Account 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 its 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.

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

- (i) maintain, in accordance with paragraph (a) of this Section, records and accounts reflecting such expenditures;
- (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 or payment out of the Special Account was made, all records (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 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 5.02. (a) Except as the Bank shall otherwise agree, the Borrower shall produce, for each of its fiscal years after its fiscal year ending on December 31, 1990, funds from internal sources equivalent to not less than 40% of the annual average of the Borrower's capital expenditures incurred, or expected to be incurred, for that year, the previous fiscal year and the next following fiscal year.

(b) Before November 30 in each of its fiscal years, the Borrower shall, on the basis of forecasts prepared by the Borrower 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 a copy of such review upon its completion.

(c) If any such review shows that the Borrower would not meet the requirements set forth in paragraph (a) for the Borrower's fiscal years covered by such review, the Borrower shall promptly take all necessary measures in order to meet such requirements.

(d) For the purposes of this Section:

(i) The term "funds from internal sources" means the difference between:

(A) the sum of revenues from all sources related to operations, consumer deposits and consumer contributions in aid of construction, net non-operating income and any reduction in working capital other than cash; and

(B) the sum of all expenses related to operations, including administration, adequate maintenance and taxes and payments in lieu of taxes (excluding provision for depreciation and other non-cash operating charges), debt service requirements, all cash dividends and other cash distributions of surplus, increase in working capital other than cash and other cash outflows other than capital expenditures.

(ii) 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.

(iii) The term "working capital other than cash" means the difference between current assets excluding cash and current liabilities at the end of each fiscal year.

(iv) The term "current assets excluding cash" means all assets other than cash 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.

- (v) The term "current liabilities" means all liabilities which will become due and payable or could under the 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.
- (vi) 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.
- (vii) The term "capital expenditures" means all expenditures incurred on account of fixed assets, including interest charged to construction, related to operations.
- (viii) 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 5.03. (a) Except as the Bank shall otherwise agree, the Borrower shall earn an annual return of not less than 18% for its fiscal year after its fiscal year ending December 31, 1990, 20% for its fiscal year after its fiscal year ending December 31, 1991 and 22% for its fiscal year ending December 31, 1992 and for each of its fiscal years thereafter, of the average current net value of the Borrower's fixed assets in operation.

(b) Before November 30 in each of its fiscal years, the Borrower shall, on the basis of forecasts prepared by the Borrower 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 the Borrower would not meet the requirements set forth in paragraph (a) for the Borrower's fiscal years covered by such review, the Borrower shall promptly take all necessary measures in order to meet such requirements.

(d) For the purposes of this Section:

- (i) The annual return shall be calculated by dividing the Borrower's net operating income for the fiscal year in question by one half of the sum of the current net value of the Borrower's fixed assets in operation at the beginning and at the end of that fiscal year.
- (ii) The term "net operating income" means total operating revenues less total operating expenses.
- (iii) The term "total operating revenues" means revenues from all sources related to operations.
- (iv) The term "total operating expenses" means all expenses related to operations, including administration, adequate maintenance, taxes and payments in lieu of taxes, and provision for depreciation on a basis acceptable to the Bank, but excluding interest and other charges on debt.
- (v) The average current gross value of the Borrower's

fixed assets in operation shall be calculated as one half of the sum of the gross value of the Borrower's fixed assets in operation at the beginning and at the end of the fiscal year, as valued from time to time in accordance with sound and consistently maintained methods of valuation satisfactory to the Bank.

- (vi) The term "current net value of the Borrower's fixed assets in operation" means the gross value of the Borrower's fixed assets in operation less the amount of accumulated depreciation, as valued from time to time in accordance with sound and consistently maintained methods of valuation satisfactory to the Bank.

Section 5.04. (a) Except as the Bank shall otherwise agree, the Borrower shall not incur any debt unless a reasonable forecast of the revenues and expenditures of the Borrower shows that the estimated net revenues of the Borrower for each fiscal year during the term of the debt to be incurred shall be at least three times the estimated debt service requirements of the Borrower in such year on all debt of the Borrower including the debt to be incurred.

(b) For the purposes 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.
- (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 payments 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 of repayments (including sinking fund payments, if any) of, and interest and other charges on, debt.
- (vi) The term "reasonable forecast" means a forecast prepared by the Borrower not earlier than twelve months prior to the incurrence of the debt in

question, which both the Bank and the Borrower accept as reasonable and as to which the Bank has notified the Borrower 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 the Borrower.

- (vii) 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.

ARTICLE VI

Remedies of the Bank

Section 6.01. Pursuant to Section 6.02 (k) of the General Conditions, the following additional event is specified, namely, that the Establishment Resolution shall have been amended, suspended, abrogated, repealed or waived so as to affect materially and adversely the ability of the Borrower to perform any of its obligations under this Agreement.

Section 6.02. Pursuant to Section 7.01 (h) of the General Conditions, the following additional event is specified, namely, that the event specified in Section 6.01 of this Agreement shall occur.

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. Except as provided in Section 2.08 of this Agreement, the General Manager of the Borrower 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 Bank:

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

Cable address:

INTBAFRAD
Washington, D.C.

Telex:

248423 (RCA),
82987 (FTCC),
64145 (WUI) or
197688 (TRT)

For the Borrower:

Hungarian Telecommunications
Company
H-1541 Budapest
Krisztina krt 6-8
Republic of Hungary

Telex:

22-1193-H

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

INTERNATIONAL BANK FOR
RECONSTRUCTION AND DEVELOPMENT

By /s/ Eugenio F. Lari
Acting Regional Vice President
Europe, Middle East and North Africa

HUNGARIAN TELECOMMUNICATIONS COMPANY

By /s/ Pal Horvath
Authorized Representative

SCHEDULE 1

Withdrawal of the Proceeds of the Loan

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 Allocated (Expressed in Dollar Equivalent) | % of Expenditures to be Financed |
|--|---|---|
| (1) Goods | 140,000,000 | 100% of foreign expenditures, 100% of local expenditures (ex-factory cost) |
| (2) Consultants' services and training | 2,000,000 | 100% |
| Unallocated | 8,000,000 | |
| TOTAL | 150,000,000 ===== | |

2. For the purposes of this Schedule:

(a) the term "foreign expenditures" means expenditures in the currency of any country other than that of the Guarantor for

goods or services supplied from the territory of any country other than that of the Guarantor; and

(b) the term "local expenditures" means expenditures in the currency of the Guarantor or for goods or services supplied from the territory of the Guarantor.

3. Notwithstanding the provisions of paragraph 1 above, no withdrawals shall be made in respect of payments made for expenditures prior to the date of this Agreement.

SCHEDULE 2

Description of the Project

The objectives of the Project are to assist the Borrower in carrying out its programs of investments and institutional development over the period 1991-1993 to rehabilitate and expand its telecommunications facilities and strengthen its management and operations.

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:

Carrying out of a program to improve and expand the Borrower's telecommunications network and facilities, including the provision and installation of (1) an overlay digital long-distance network; (2) international telecommunications network, including Intelsat and Eutelsat ground stations, gateway exchange, international telephone circuits and telex and data circuits; (3) local switching capacity and associated local networks and subscriber plant for connection of new subscribers, the majority of which will be high-volume business subscribers; (4) rural network fiber optic and microwave transmission systems; (5) an expanded mobile radio telephone network; (6) expanded telex and data services; and (7) public card pay phones.

Part B:

Carrying out of a program to strengthen the Borrower's organization, management and operations, including:

(1) development and implementation of: (a) a comprehensive master plan for the management and development of human resources and the streamlining of organizational structures; (b) suitable management information, accounting and staff incentive systems to increase efficiency and productivity; (c) a suitable marketing strategy and a competitive procurement system; (d) an optimal digitalization strategy; (e) a program of defined measures to improve the efficiency of investments in network expansion and of the utilization of existing network; and

(2) provision of studies to develop appropriate strategies for further automatization of telephone operations, development of new telecommunications services, rationalization of telecommunications tariffs, expansion of telephone services provided through special arrangements with customers' associations and upgrading of operational policies based on transparent performance criteria; and

(3) provision of management and staff training in the management of commercial telecommunications operations and in the applications of modern telecommunications technology.

* * *

The Project is expected to be completed by December 31, 1995.

SCHEDULE 3

Amortization Schedule

| Date Payment Due | Payment of Principal (expressed in dollars)* |
|---|---|
| On each May 15 and November 15 beginning May 15, 1996 through November 15, 2005 | 7,500,000 |

* The figure in this column represents the dollar equivalent determined as of the respective dates of withdrawal. See General Conditions, Sections 3.04 and 4.03.

Premiums on Prepayment

Pursuant to Section 3.04 (b) of the General Conditions, the premium payable on the principal amount of any maturity of the Loan to be prepaid shall be the percentage specified for the applicable time of prepayment below:

| Time of Prepayment | Premium |
|---|---|
| | The interest rate (expressed as a percentage per annum) applicable to the Loan on the day of prepayment multiplied by: |
| Not more than three years before maturity | 0.20 |
| More than three years but not more than six years before maturity | 0.40 |
| More than six years but not more than 11 years before maturity | 0.73 |
| More than 11 years but not more than 13 years before maturity | 0.87 |
| More than 13 years before maturity | 1.00 |

SCHEDULE 4

Procurement and Consultants' Services

Section I. Procurement of Goods and Works

Part A: International Competitive Bidding

Except as provided in Part C hereof, goods 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 Guarantor's territory, 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

1. Goods, including technical licenses, estimated to cost the equivalent of \$300,000 or less per contract, up to an aggregate amount equivalent to \$5,000,000, may be procured under contracts awarded on the basis of comparison of price quotations obtained from at least three suppliers from at least two different countries eligible under the Guidelines, in accordance with procedures acceptable to the Bank.

2. Goods, including technical licenses, which the Bank agrees (a) are of proprietary nature, (b) the timely supply thereof is critical for efficient Project execution, or (c) need to be compatible with other installed equipment, may be awarded after direct negotiations with suppliers, in accordance with procedures acceptable to the Bank.

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, said 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 5 to this Agreement.

(c) The provisions of the preceding subparagraph (b) shall not apply to contracts on account of which the Bank has authorized withdrawals on the basis of statements of expenditure.

2. The figure of 15% is hereby specified for purposes of paragraph 4 of Appendix 1 to the Guidelines.

Section II. Employment of Consultants

Consultants' services shall be procured under contracts awarded to: (A) consultants whose qualifications, experience and terms and conditions of employment shall be satisfactory to the Bank; and (B) who 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 5

Special Account

1. For the purposes of this Schedule:

(a) the term "eligible Categories" means Categories (1) and (2) set forth in the table in paragraph 1 of Schedule 1 to this Agreement;

(b) the term "eligible expenditures" means expenditures in respect of the reasonable cost of goods and services required for

the Project and to be financed out of the proceeds of the Loan allocated from time to time to the eligible Categories in accordance with the provisions of Schedule 1 to this Agreement; and

(c) the term "Authorized Allocation" means an amount equivalent to \$10,000,000 to be withdrawn from the Loan Account and deposited in the Special Account pursuant to paragraph 3 (a) of this Schedule.

2. Payments out of the Special Account shall be made exclusively for eligible expenditures in accordance with the provisions of this Schedule.

3. After the Bank has received evidence satisfactory to it that the Special Account has been duly opened, withdrawals of the Authorized Allocation 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 a deposit or deposits which do not exceed the aggregate amount of the Authorized Allocation. On the basis of such request or requests, the Bank shall, on behalf of the Borrower, withdraw from the Loan Account and deposit in the Special Account such amount or amounts as the Borrower shall have requested.

(b) (i) For replenishment of the Special Account, the Borrower shall furnish to the Bank requests for deposits into the Special Account at such intervals as the Bank shall specify.

(ii) 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 paragraph 4 of this Schedule 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.

All such deposits shall be withdrawn by the Bank from the Loan Account under the respective eligible Categories, and in the respective equivalent amounts, as shall have been justified by said documents and other evidence.

4. 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.

5. Notwithstanding the provisions of paragraph 3 of this Schedule, the Bank shall not be required to make further deposits into the Special Account:

(a) if, at any time, the Bank shall have determined that all further withdrawals should be made by the Borrower directly from the Loan Account in accordance with the provisions of Article V of the General Conditions and paragraph (a) of Section 2.02 of this Agreement; or

(b) once the total unwithdrawn amount of the Loan allocated to the eligible Categories, less the amount of any outstanding special commitment entered into by the Bank pursuant to Section 5.02 of the General Conditions with respect to the Project, 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 allocated to the eligible Categories 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.

6. (a) If the Bank shall have determined at any time that any payment out of the Special Account: (i) was made for an expenditure or in an amount not eligible pursuant to paragraph 2 of this Schedule; or (ii) was not justified by the evidence furnished to the Bank, the Borrower shall, promptly upon notice from the Bank: (A) provide such additional evidence as the Bank may request; or (B) 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 or the portion thereof not so eligible or justified. 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 shall have determined at any time that any amount outstanding in the Special Account will not be required to cover further payments for eligible expenditures, 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 paragraphs 6 (a), (b) and (c) of this Schedule shall be credited to the Loan Account for subsequent withdrawal or for cancellation in accordance with the relevant provisions of this Agreement, including the General Conditions.

SCHEDULE 6

Action Plan Outline

The Action Plan describes the program of objectives, policies and actions designated to facilitate the efficient implementation of the Borrower's institutional development strategy to further develop its organization, management and operations. It indicates the measures to be undertaken by the Borrower pursuant to the Action Plan and the time frame within which these measures will be initiated and completed. It includes, inter alia:

(1) the measures to define and incorporate in a formal corporate plan, and, thereafter, achieve the Borrower's institutional, strategic and operational objectives and policies, including those relating to (a) the implementation of a detailed strategy for improving the process of consultation and coordination with other enterprises operating within the Guarantor's telecommunications manufacturing subsector and for fostering competition within said subsector through the adoption and application of suitable competitive procurement policies, including the gradual introduction of a competitive purchasing process which will ensure that, by December 31, 1993, the percentage of purchases subject to such competitive process, within the overall purchases of the Borrower in any fiscal year, shall be at least twice the percentage of the purchase subjected to such a competitive process during the twelve months period preceding the date of this Agreement, (b) the establishment and operation of separate commercial offices based on service and customers classes, including the implementation of an action plan to ascertain on a regular basis, and effectively respond to, the needs for telecommunications services of high volume business and other subscriber communities, and the establishment and maintenance of suitable special offices for these purposes, and (c) the design and implementation of measures required for the efficient commercialization of operations, inter alia, to facilitate the privatiza-

tion of such operations, including the conclusion of twinning arrangements with international telecommunications companies to advance these objectives;

(2) the measures to develop and implement a plan for improving the Borrower's operational efficiency, including the reduction of the operational cost (excluding depreciation) of direct exchange telephone lines and of the number of workers employed in the operation of the same;

(3) the measures to develop and implement a plan for improving the quality of services provided by the Borrower, including the reduction of the number of faulty telephones service, the shortening of the time required to repair faulty telephone services, and the increasing of the composite quality of service index;

(4) the measures to develop and implement a plan for improving the Borrower's investment efficiency, including the reduction of the equipment unit cost of installed capacity, shortening the time of construction and capacity installation and reduction of installation labor cost;

(5) the procedures to develop and carry out plans of action to achieve the objectives of the studies provided under Part B (2) of the Project in accordance with the provision of Section 4.02 of this Agreement; and

(6) the procedures to monitor, evaluate, update and carry out the specific measures required to ensure the achievement of the objectives of the Action Plan in accordance with the provisions of Section 4.01 (b) of this Agreement.

