

Public Disclosure Authorized

CONFORMED COPY

LOAN NUMBER 4205 HU

Loan Agreement

(Quick Start Gas Turbine Project)

between

**INTERNATIONAL BANK FOR RECONSTRUCTION
AND DEVELOPMENT**

and

HUNGARIAN POWER COMPANIES LTD.

Dated July 2, 1997

LOAN NUMBER 4502 HU

LOAN AGREEMENT

AGREEMENT, dated July 2, 1997 between INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT (the Bank) and HUNGARIAN POWER COMPANIES LTD. (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 for Single Currency Loans" of the Bank, dated May 30, 1995 (the General Conditions) with the modifications set forth below constitute an integral part of this Agreement:

(a) Section 6.03 is modified to read:

"Section 6.03. Cancellation by the Bank. If (a) the right of the Borrower to make withdrawals from the Loan Account shall have been suspended with respect to any amount of the Loan for a continuous period of thirty days, or (b) at any time, the Bank determines, after consultation with the Borrower, that an amount of the Loan will not be required to finance the Project's costs to be financed out of the proceeds of the Loan, or (c) at any time, the Bank determines, with respect to any contract to be financed out of the proceeds of the Loan, that corrupt or fraudulent practices were engaged in by representatives of the Borrower or of a beneficiary of the Loan during the procurement or the execution of such contract, without the Borrower having taken timely and

appropriate action satisfactory to the Bank to remedy the situation, and establishes the amount of expenditures in respect of such contract which would otherwise have been eligible for financing out of the proceeds of the Loan, or (d) at any time, the Bank determines that the procurement of any contract to be financed out of the proceeds of the Loan is inconsistent with the procedures set forth or referred to in the Loan Agreement and establishes the amount of expenditures in respect of such contract which would otherwise have been eligible for financing out of the proceeds of the Loan, or (e) after the Closing Date, an amount of the Loan shall remain unwithdrawn from the Loan Account, or (f) the Bank shall have received notice from the Guarantor pursuant to Section 6.07 with respect to an amount of the Loan, the Bank may, by notice to the Borrower and the Guarantor, terminate the right of the Borrower to make withdrawals with respect to such amount. Upon the giving of such notice, such amount of the Loan shall be cancelled.”

Section 1.02. Unless the context otherwise requires, the several terms defined in the General Conditions have the respective meanings therein set forth and the following additional term has the following meaning, namely “FY” means the fiscal year of the Borrower, being the calendar year.

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 sixty million Dollars (\$60,000,000).

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 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 June 30, 1999, 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 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 2.06 of this Agreement.
- (iii) “LIBOR Base Rate” means, for each Interest Period, the London interbank offered rate for six-month deposits in Dollars 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) one-half of one percent (1/2 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 Guarantor and Borrower 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 2.05, 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 of the new basis. The basis shall become effective on the expiry of the notice period unless the Borrower notifies the Bank during said period of its objection thereto, in which case said modification shall not apply to the Loan.

Section 2.06. Interest and other charges shall be payable March 15 and September 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.

ARTICLE III

Execution of the Project

Section 3.01. 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 public utility practices and shall provide, promptly as needed, the funds, facilities, services and other resources required for the Project.

Section 3.02. Except as the Bank shall otherwise agree, procurement of the goods 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 3.03. For the purposes of Section 9.08 of the General Conditions and without any 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 Bank and the Borrower, 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 3.04. The Borrower shall:

(a) maintain policies and procedures adequate to enable it to monitor and evaluate on an ongoing basis, in accordance with indicators agreed with 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 January 30, 1998 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, 1998, 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 the Bank views on the matter.

ARTICLE IV

Management and Operations of the Borrower

Section 4.01. (a) The Borrower shall carry on its operations and conduct its affairs in accordance with sound administrative, financial, engineering and public utility practices under the supervision of qualified and experienced management assisted by competent staff in adequate numbers.

(b) The Borrower shall take all measures as shall be consistent with the monitoring program specified in the environmental assessment, dated June 6, 1996, and take proper actions to monitor the noise levels of the power plants constructed under the Project.

Section 4.02. The Borrower shall 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 and financial practices.

Section 4.03. 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, statement of sources and application of funds and related statements), the consolidated accounts of the Borrower and its subsidiaries and the records and accounts for each FY 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 June 15 of each year in the case of the Borrower's records, accounts and financial statements and, in the case of the consolidated accounts of the Borrower and its subsidiaries, no later than August 31 in FY 1997, July 31 in FY 1998 and June 15 each FY thereafter: (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 FY in which the last withdrawal from the Loan 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 FY, 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 generate, during FY 1998, 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 FY and the next following FY; such ratio to be 55% during each FY thereafter.

(b) Before April 30 and October 1 in each of its fiscal year, 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 (including, without limitation, initiating and, upon receiving necessary authorization, implementing 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 "funds from internal sources" means the difference between:

(A) the sum of revenues from all sources related to operations, debt service due from affiliates, 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 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 of this Agreement 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 maintain a ratio of current assets to current liabilities of not less than 1.0.

(b) Before July 1 in each of its FYs, 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 FY 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 FYs covered by such review, the Borrower shall promptly take all necessary measures in order to meet such requirement.

(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 FY.
- (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 5.04. (a) Except as the Bank shall otherwise agree, the Borrower shall not incur any debt, unless the net revenues of the Borrower for the FY immediately preceding the date of such incurrence or for a later twelve-month period ended prior to the date of such incurrence, whichever is the greater, shall be at least 1.5 times the estimated maximum debt service requirements of the Borrower for any succeeding FY 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 adjusted to take account of the Borrower’s rates in effect at the time of the incurrence of debt even though they were not in effect during the twelve-month period to which such revenues relate 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 amount of repayments (including sinking fund payments, if any) of, and interest and other charges on, debt, minus any such repayment and interest payments in respect of debt incurred by the Borrower and onlent to any of its affiliate companies.
- (vi) 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 5.05. The provisions of this Article V shall supersede all previous undertakings of the Borrower in respect of financial covenants set forth in the Project Agreement for the Power Project dated June 17, 1986 (Loan No. 2697 HU) and in the Loan Agreement for the Energy and Environment Project dated March 25, 1994 (Loan No. 3705 HU).

ARTICLE VI

Termination

Section 6.01. 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 VII

Representative of the Borrower; Addresses

Section 7.01. The Director for Strategy and Development of the Borrower is designated as representative of the Borrower for the purposes of Section 11.03 of the General Conditions.

Section 7.02. 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:

Telex:

INTBAFRAD
Washington, D.C.

248423 (MCI)
64145 (MCI)

For the Borrower:

Hungarian Power Companies Ltd.
Vam utca 5-7
H-1011 Budapest
Republic of Hungary

Telex:

22-4382 MVM 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 Budapest, Hungary, as of the day and year first above written.

INTERNATIONAL BANK FOR
RECONSTRUCTION AND DEVELOPMENT

By /s/ Millard Long

Acting Regional Vice President
Europe and Central Asia

HUNGARIAN POWER COMPANIES LTD.

By /s/ Antal Tomboz

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:

<u>Category</u>	<u>Amount of the Loan Allocated (Expressed in Dollars)</u>	<u>% of Expenditures to be Financed</u>
(1) Goods	60,000,000	100% of foreign expenditures, 100% of local expenditures (ex-factory cost) and 75% of local expenditures for other items procured locally

TOTAL	60,000,000	
	=====	

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, except that withdrawals, in an aggregate amount not exceeding the equivalent of \$7,500,000 may be made on account of payments made for expenditures before that date but after January 1, 1997.

SCHEDULE 2

Description of the Project

The objective of the Project is to assist the Borrower in establishing the quick start electric power generating capacity needed for the Borrower's interconnection with the West European power pool.

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

Construction of two complete simple cycle gas turbine power plants (about 110 MW each) in Liter and Sajoszoged, including:

1. Provision and installation of: (i) gas turbine generating sets and auxiliaries, air inlet and exhaust gas systems; (ii) electrical equipment, as required to serve plants needs; (iii) power plant control system; (iv) high voltage switchgear and unit transformers to connect the generator sets to the 120 KV system; and (v) enclosures and light structure to accommodate the gas turbine units and auxiliaries.
2. Installation of an auxiliary system, including: (i) fuel supply system, including unloading facilities, oil storage tanks, and pumping stations and piping; (ii) demineralized water supply for make-up cooling water; (iii) water supply for fire extinguishing system; (iv) fire detection and protection system; and (v) telecommunications and remote control and indication system.
3. Carrying out of works, including: (i) site preparation, leveling and earthwork; (ii) foundations for main equipment enclosures and buildings; (iii) foundations for auxiliary equipment and storage tanks; and (iv) site improvements, cable and piping channels and trenches.
4. Connections to integrate the plant with the Borrower's energy management system.

* * *

The Project is expected to be completed by December 31, 1998.

SCHEDULE 3

Amortization Schedule

<u>Date Payment Due</u>	<u>Payment of Principal (Expressed in Dollars)*</u>
On each March 15 and September 15 beginning September 15, 2002 through March 15, 2012	3,000,000

* The figure in this column represents the amount in Dollars to be repaid except as provided in Section 4.04 (d) of the General Conditions.

SCHEDULE 4

Procurement

Part A: General

Goods 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 (the Guidelines) and the following provisions of this Section, as applicable.

Part B: International Competitive Bidding

1. The design, supply and installation of gas turbine generating sets and auxiliary system together with related civil works shall be procured under a single contract 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 the contract referred to in paragraph 1 of this Part B and awarded in accordance with the provisions thereof.

(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 Borrower.

(b) Notification and Advertising

The invitation to prequalify or bid for the contract referred to in paragraph 1 of this Part B shall be advertised in accordance with the procedures applicable to large contracts under paragraph 2.8 of the Guidelines.

Part C: Review by the Bank of Procurement Decisions

1. Procurement Planning

Prior to the issuance of an invitation to prequalify for bidding or to bid for the contracts referred to in paragraph B.1 of this Schedule, 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

The procedures set forth in paragraphs 2 and 3 of Appendix 1 to the Guidelines shall apply to the contract referred to in paragraph B.1 of this Schedule.