

CONFORMED COPY

LOAN NUMBER 4705-CHA

Project Agreement

(Shanghai Urban Environment Project)

between

**INTERNATIONAL BANK FOR RECONSTRUCTION
AND DEVELOPMENT**

and

SHANGHAI MUNICIPALITY

Dated November 10 , 2003

LOAN NUMBER 4705-CHA

PROJECT AGREEMENT

AGREEMENT, dated November 10 , 2003 , between INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT (the Bank) and SHANGHAI MUNICIPALITY (Shanghai).

WHEREAS by the Loan Agreement of even date herewith between People's Republic of China (the Borrower) and the Bank, the Bank has agreed to make a loan to the Borrower in the amount of two hundred million Dollars (\$200,000,000) on the terms and conditions set forth in the Loan Agreement, but only on condition that Shanghai agree to undertake such obligations toward the Bank as are set forth in this Agreement; and

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

NOW THEREFORE the parties hereto hereby agree as follows:

ARTICLE I

Definitions

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

ARTICLE II

Execution of the Project

Section 2.01. (a) Shanghai declares its commitment to the objectives of the Program and of the Project as set forth in Schedule 2 to the Loan Agreement, and, to this end, shall carry out, and shall cause to be carried out, the Project with due diligence and efficiency and in conformity with appropriate administrative, financial, engineering and public utility practices, and social and environmental standards acceptable to the Bank, and shall provide, or cause to be provided, promptly as needed, the funds, facilities, services and other resources required for the Project.

(b) Without limitation upon the provisions of paragraph (a) of this Section and except as the Bank and Shanghai shall otherwise agree, Shanghai shall carry out, and shall cause to be carried out, the Project in accordance with the Implementation Program set forth in Schedule 2 to this Agreement.

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

Section 2.03. (a) Shanghai shall carry out, and shall cause to be carried out, the obligations set forth in Sections 9.04, 9.05, 9.06, 9.07, 9.08 and 9.09 of the General Conditions (relating to insurance, use of goods and services, plans and schedules, records and reports, maintenance and land acquisition, respectively) in respect of this Agreement.

(b) For the purposes of Section 9.07 of the General Conditions and without limitation thereto, Shanghai shall:

- (i) prepare, on the basis of guidelines acceptable to the Bank, and furnish to the Bank not later than six (6) months before the Closing Date or such later date as may be agreed for this purpose between the Bank and Shanghai, a plan for the continued achievement of the objectives of the Project; and
- (ii) afford the Bank a reasonable opportunity to exchange views with Shanghai on said plan.

Section 2.04 (a) Shanghai shall, at the request of the Bank, exchange views with the Bank with regard to progress of the Program and the Project, the performance of its obligations under this Agreement and other matters relating to the purposes of the Loan.

(b) Shanghai shall promptly inform the Bank of any condition which interferes or threatens to interfere with the progress of the Project, the accomplishment of the purposes of Loan, or the performance by Shanghai of its obligations under this Agreement.

ARTICLE III

Financial Covenants

Section 3.01. (a) Shanghai shall maintain, and shall cause to be maintained, records and accounts adequate to reflect in accordance with sound accounting practices the operations, resources and expenditures in respect of the Project of the departments or agencies of Shanghai and of each of the Participating Districts, responsible for carrying out the Project or any part thereof.

- (b) Shanghai shall:
- (i) have the records and accounts referred to in paragraph (a) of this Section 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 (6) months after the end of each such year 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 and accounts and the audit thereof as the Bank shall from time to time reasonably request.

Section 3.02. (a) Without limitation upon Shanghai's progress reporting obligations set out in paragraph 15 of Schedule 2 to this Agreement, Shanghai shall prepare and furnish to the Bank financial monitoring reports, in form and substance satisfactory to the Bank, which set forth sources and uses of funds for the Project, both cumulatively and for the period covered by each said report, showing separately funds provided under the Loan, and explain variances between the actual and planned uses of such funds.

(b) The first such financial management report shall be furnished to the Bank not later than 45 days after the end of the first calendar semester after the Effective Date, and shall cover the period from the incurrence of the first expenditure under the Project through the end of such first calendar semester; thereafter, each financial management report shall be furnished to the Bank not later than 45 days after each subsequent calendar semester, and shall cover such calendar semester.

ARTICLE IV

Effective Date; Termination;

Cancellation and Suspension

Section 4.01. This Agreement shall come into force and effect on the date upon which the Loan Agreement becomes effective.

Section 4.02. This Agreement and all obligations of the Bank and of Shanghai thereunder shall terminate on the date on which the Loan Agreement shall terminate in accordance with its terms, and the Bank shall promptly notify Shanghai thereof.

Section 4.03. All the provisions of this Agreement shall continue in full force and effect notwithstanding any cancellation or suspension under the General Conditions.

ARTICLE V

Miscellaneous Provisions

Section 5.01. Any notice or request required or permitted to be given or made under this Agreement and any agreement between the parties contemplated by this Agreement shall be in writing. Such notice or request shall be deemed to have been duly given or made when it shall be delivered by hand or by mail, telex or facsimile to the party to which it is required or permitted to be given or made at such party's address hereinafter specified or at such other address as such party shall have designated by notice to the party giving such notice or making such request. Deliveries made by facsimile transmission shall also be confirmed by mail. The addresses so specified are:

For the Bank:

International Bank for
Reconstruction and Development
1818 H Street, NW
Washington, DC 20433
United States of America

Cable address:	Telex:	Facsimile:
INTBAFRAD Washington, D.C.	248423 (MCI) or 64145 (MCI)	(1-202) 477-6391

For Shanghai:

200 Renmin Da Dao
Shanghai, 200003

P.R. China

Facsimile:
86-21 6311 9462/86-21 5652 9502

Section 5.02. Any action required or permitted to be taken, and any document required or permitted to be executed, under this Agreement on behalf of Shanghai may

be taken or executed by its Mayor or a Vice Mayor or such other person or persons as said Mayor or Vice Mayor shall designate in writing, and Shanghai shall furnish to the Bank sufficient evidence of the authority and the authenticated specimen signature of each such person.

Section 5.03. This Agreement may be executed in several counterparts, each of which shall be an original, and all collectively but one instrument.

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

INTERNATIONAL BANK FOR
RECONSTRUCTION AND DEVELOPMENT

By /s/ Yukon Huang
Authorized Representative

SHANGHAI MUNICIPALITY

By /s/ Zou Jiayi
Authorized Representative

SCHEDULE 1

Procurement

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 Section I of this Schedule.

Part B: International Competitive Bidding

1. Except as otherwise provided in Part C of this Section, 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 Borrower (other than goods manufactured in the Hong Kong Special Administrative Region or the Macau Special Administrative Region of the Borrower).

(b) Dispute Review Board

Each contract for works estimated to cost \$50,000,000 equivalent or more shall include the provisions for a dispute review board set forth in the standard bidding documents for works referred to in paragraph 2.12 of the Guidelines.

(c) 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 Procedure

National Competitive Bidding

(a) Goods estimated to cost less than \$500,000 equivalent per contract, up to an aggregate amount not to exceed \$1,500,000 equivalent, and works estimated to cost less than \$10,000,000 equivalent per contract up to an aggregate amount not to exceed \$273,000,000 equivalent, may be procured under contracts awarded in accordance with the provisions of paragraphs 3.3 and 3.4 of the Guidelines.

(b) The procedures to be followed for National Competitive Bidding under Part C.1 of this Section shall be those set forth in the Law on Tendering and Bidding of the People's Republic of China promulgated by Order No. 21 of the President of the People's Republic of China on August 30, 1999, with the following clarifications required for compliance with the Guidelines:

- (i) All invitations to prequalify or to bid shall be advertised in a newspaper of national circulation in China and such advertisement shall be made in sufficient time for prospective bidders to obtain prequalification or bidding documents and prepare and submit their responses. In any event, a minimum of thirty (30) days shall be given to bidders between the date of advertisement in such newspaper and the deadline for submission of bids, and the advertisement and bidding documents shall specify the deadline for such submission.
- (ii) Qualification requirements of bidders and the method of evaluating the qualification of each bidder shall be specified in detail in the bidding documents.
- (iii) All bidders shall be required to provide security in an amount sufficient to protect the Borrower, in case of breach of contract by the contractor, and the bidding documents shall specify the required form and amount of such security.
- (iv) The time for opening of all bids shall be the same as the deadline for receipt of such bids.
- (v) All bids shall be opened in public; all bidders shall be afforded an opportunity to be present (either in person or through their representatives) at the time of bid opening, but bidders shall not be required to be present at the bid opening.

- (vi) No bid may be rejected solely on the basis that the bid price falls outside any standard contract estimate, or margin or bracket of average bids established by the Borrower.
- (vii) Each contract shall be awarded to the lowest evaluated responsive bidder, that is, the bidder who meets the appropriate standards of capability and resources and whose bid has been determined (A) to be substantially responsive to the bidding documents and (B) to offer the lowest evaluated cost. The winning bidder shall not be required, as a condition of award, to undertake responsibilities for work not stipulated in the bidding documents or otherwise to modify the bid as originally submitted.
- (viii) Each contract financed with the proceeds of the Loan shall provide that the suppliers and contractors shall permit the Bank, at its request, to inspect their accounts and records relating to the performance of the contract and to have said accounts and records audited by auditors appointed by the Bank.

Part D: Review by the Bank of Procurement Decisions

1. Procurement Planning

Prior to the issuance of any invitations 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 for (a) works estimated to cost the equivalent of \$10,000,000 or more, and (b) goods estimated to cost the equivalent of \$500,000 or more, 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 Sections I and 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, January 1999 and May 2002 (the Consultant Guidelines), paragraph 1 of Appendix 1 thereto, Appendix 2 thereto, and the following provisions of this Section.

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, 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

1. Quality-based Selection

Services for a study on pollution reduction measures under Part F.2 of the Project may be procured under contracts awarded in accordance with the provisions of paragraphs 3.1 through 3.4 of the Consultant Guidelines.

2. Selection Under a Fixed Budget

Services for studies on alternative funding for environmental services under Part F.2 of the Project, and for provision of training may be procured under contracts awarded in accordance with the provisions of paragraphs 3.1 and 3.5 of the Consultant Guidelines.

3. Selection Based on Consultants' Qualifications

Services under Parts B and C of the Project, and services for the development of procurement procedures for private sector participation under Part F.2 of the Project may be procured under contracts awarded in accordance with the provisions of paragraphs 3.1 and 3.7 of the Consultant Guidelines.

4. Single Source Selection

Services which are estimated to cost less than \$100,000 equivalent per contract, may, with the Bank's prior agreement, be procured in accordance with the provisions of paragraphs 3.8 through 3.11 of the Consultant Guidelines.

5. Individual Consultants

Services for tasks that meet the requirements set forth in paragraph 5.1 of the Consultant Guidelines may be procured under contracts awarded to individual consultants in accordance with the provisions of paragraphs 5.1 through 5.3 of the Consultant Guidelines.

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

1. Selection Planning

A plan for the selection of consultants, which shall include contract cost estimates, contract packaging, and applicable selection criteria and procedures, shall be furnished to the Bank for its review and approval, prior to the issuance to consultants of any requests for proposals. Selection of all consultants' services shall be undertaken in accordance with such selection plan as shall have been approved by the Bank.

2. Prior Review

(a) 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 2, 3 and 5 of Appendix 1 to the Consultant Guidelines shall apply.

(b) With respect to each contract for the employment of individual consultants estimated to cost the equivalent of \$50,000 or more, the report on the comparison of the qualifications and experience of candidates and the terms of reference and terms of employment of the consultants shall be furnished to the Bank for its prior review and approval. The contract shall be awarded only after the said approval shall have been given. The provisions of paragraph 3 of Appendix 1 to the Consultant Guidelines shall also apply to such contracts.

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 Consultant Guidelines shall apply.

SCHEDULE 2

Implementation Program

Project Management

1. Throughout the period of implementation of the Project, Shanghai shall maintain:

(a) the Program Leading Group to provide overall guidance and coordination in the implementation of the Program and the Project and to monitor progress in the overall urban environment improvement strategy; and

(b) the Project Office, under the direction of qualified and experienced managers, staffed with competent personnel in sufficient numbers, and provided with adequate resources, to be responsible for the overall management, supervision, monitoring and evaluation of, and reporting on Project activities, including the management of procurement, and for the coordination among all implementation entities.

2. Shanghai shall cause each Project implementing entity, as set forth in Section 1.03 of the Loan Agreement, to establish and, thereafter throughout the period of implementation of the Project, maintain its respective project management office, under the direction of qualified and experienced managers and staffed with competent personnel in sufficient numbers, and provided with adequate resources; said project management office to be responsible for the overall management, supervision and monitoring of the implementation of its respective part of the Project.

Resettlement and Environment Protection

3. Shanghai shall:

(a) take, and shall cause SMSC, Chengtou, the Participating Districts and their Respective Sewerage Companies to take, all necessary actions to minimize to the extent possible any involuntary loss by persons of shelter, productive assets or access to productive assets or income or means of livelihood, temporarily or permanently;

(b) for this purpose, implement, and cause SMSC, Chengtou, the Participating Districts and their Respective Sewerage Companies to implement, the Resettlement Action Plans in a manner satisfactory to the Bank; and

(c) prepare, or shall cause to be prepared, resettlement action plans in regard to Part C of the Project, satisfactory to the Bank, in accordance with the principles and procedures set forth in the Resettlement Policy Framework, and carry out, and cause to be carried out, such resettlement action plans in a manner satisfactory to the Bank, before commencing works for the pilot urban upgrading program in Hongkou District under said Part C of the Project.

4. (a) Shanghai shall, and shall cause SMSC, Chengtou, the Participating Districts and their Respective Sewerage Companies to implement the Environmental Management Plan in a manner satisfactory to the Bank and designed to ensure that the Project is implemented in accordance with sound environmental practices and standards.

(b) Until adequate sludge treatment facilities are constructed in the Participating Districts, Shanghai shall cause said Districts and their Respective Sewerage Companies to dispose of sludge resulting from wastewater treatment safely, on site, and not to make such sludge available to farmers inside or outside of said Districts.

5. Shanghai shall, and shall cause SMSC, Chengtou, the Participating Districts and their Respective Sewerage Companies to:

(a) maintain policies and procedures adequate to enable them to monitor and evaluate, in accordance with guidelines acceptable to the Bank, the implementation of the Environmental Management Plan, the Resettlement Action Plans, and the achievement of the objectives of said Plans, including the engagement of experienced and qualified independent monitoring agencies acceptable to the Bank;

(b) include the results of such monitoring and evaluation activities in each report referred to in paragraphs (6)(j) and (9)(j) below, together with any revisions proposed to be introduced into such Plans in order to achieve their respective objectives; and

(c) introduce such revisions into such Plans as shall have been agreed with the Bank.

Project Implementation

6. For purposes of Part A of the Project, Shanghai shall re-lend to SMSC a portion of the Loan proceeds made available to it, pursuant to a Subsidiary Loan Agreement acceptable to the Bank, and under terms and conditions satisfactory to the Bank which shall include, without limitation, the following:

- (a) (i) The principal amount so re-lent to SMSC shall be the amount in Dollars (on the date, or respective dates, of withdrawal from the Loan Account or paid from the Special Account) of the value of the currency or currencies so withdrawn, or paid, on account of expenditures under Categories (1)(a), (2)(a), (3)(a) and (4)(a);
- (ii) Shanghai shall recover the principal amount so made available, together with an amount equal to one percent (1%) of such principal amount, over a period of fifteen (15) years inclusive of a grace period of five (5) years;

- (iii) Shanghai shall charge interest on such principal amount, withdrawn and outstanding from time to time at a rate equal to the rate of interest applicable from time to time to the Loan pursuant to Section 2.06 of the Loan Agreement; and
- (iv) Shanghai shall charge a commitment charge on such principal amount, not withdrawn from time to time at a rate equal to three fourths of one percent ($3/4$ of 1%) per annum.

(b) SMSC shall undertake to: (i) carry out its Respective Parts of the Project, through a contractual arrangement with SWEC, with due diligence and efficiency and in accordance with appropriate management, financial, engineering and public utility practices and social and environmental standards acceptable to the Bank, and provide, promptly as needed, the funds, facilities and other resources required for the purpose; and (ii) without limitation on the foregoing, take all measures necessary to ensure that SMSC's Respective Parts of the Project shall be implemented in accordance with the Resettlement Action Plan for Shanghai Sewerage Project Phase III, and with the Environmental Management Plan.

(c) SMSC shall undertake to procure the goods, works and consultants' services for its Respective Parts of the Project and to be financed out of the proceeds of the Loan, in accordance with the provisions of Schedule 1 to this Agreement, and utilize such goods, works and consultants' services exclusively in the carrying out of said Parts of the Project.

(d) SMSC shall undertake to enable Shanghai and the Bank to inspect such goods and the sites and works included in SMSC's Respective Parts of the Project, the operation thereof, and any relevant records and documents.

(e) SMSC shall undertake to take out and maintain with responsible insurers such insurance, against such risks and in such amounts, as shall be consistent with sound business practice, including, without limitation, such insurance to cover hazards incident to the acquisition, transportation and delivery of goods financed out of the proceeds of the Loan to the place of use or installation, any indemnity thereunder to be made payable in a currency freely usable by SMSC to replace or repair such goods.

(f) SMSC shall undertake to:

- (i) maintain records and accounts adequate to reflect in accordance with sound accounting practices its operations and financial condition;
- (ii) have its financial statements (balance sheets, statements of income and expenses and related statements) for each fiscal year audited, in accordance with appropriate auditing principles

consistently applied, by independent auditors acceptable to the Bank;

- (iii) furnish to the Bank and to Shanghai, as soon as available, but in any case not later than six (6) months after the end of each such year certified copies of said financial statements and accounts for such year as so audited; the report of such audit by said auditors in such scope and detail as the Bank or Shanghai shall have reasonably requested; and all such other information concerning said records, accounts and financial statements, as well as the audit thereof, as the Bank or Shanghai shall reasonably request.

(g) SMSC shall undertake to produce for each fiscal year, commencing in 2004, total revenues equivalent to not less than the sum of:

- (i) its total operating expenses (including for maintenance) before depreciation;
- (ii) the amount by which debt service requirements exceeds the provision for depreciation;
- (iii) increases in working capital other than cash; and
- (iv) ten percent (10%) of its average capital expenditures over a rolling three-year period.

(h) SMSC shall undertake to:

- (i) review by September 30 in each fiscal year commencing in 2004, on the basis of forecasts prepared in a manner satisfactory to the Bank, whether it would meet the requirements set forth in subparagraph (g) above, in respect of such year and the next following fiscal year and furnish to the Bank the results of such review upon its completion; and
- (ii) if any such review shows that it would not meet the requirements set forth in subparagraph (g) above for the fiscal years covered by such review, promptly take all necessary measures (including, without limitation, adjustments of the structure or levels of its tariffs) in order to meet such requirements.

(i) SMSC shall undertake not to incur any debt unless a reasonable forecast of its revenues and expenditures shows that its estimated net revenues for each fiscal year during the term of the debt to be incurred shall be at least 1.3 times its estimated debt service requirements in such year on all of its debt including the debt to be incurred.

- (j) SMSC shall undertake to:
 - (i) maintain policies and procedures adequate to enable it to monitor and evaluate on an ongoing basis, in accordance with indicators satisfactory to the Bank and to Shanghai the carrying out of its Respective Parts of the Project and the achievement of the objectives thereof; and
 - (ii) prepare, under terms of reference satisfactory to the Bank and to Shanghai, and submit to the Project Office semi-annual reports integrating the results of the monitoring and evaluation activities performed pursuant to clause (i) of this subparagraph (j) on the progress achieved in the carrying out of its Respective Parts of the Project during the period preceding the date of each such report.

7. Shanghai shall: (a) exercise its rights under the Subsidiary Loan Agreement with SMSC in such manner as to protect the interests of the Borrower, the Bank and Shanghai, and to accomplish the purposes of the Loan; and (b) except as the Bank shall otherwise agree, not assign, amend, abrogate or waive its Subsidiary Loan Agreement with SMSC or any provision thereof.

8. Shanghai shall cause SMSC, to engage the services of a consultancy firm acceptable to the Bank, under terms of reference satisfactory to the Bank to assist SMSC in construction management in respect of its Respective Parts of the Project.

9. For purposes of Parts D.2, D.3 and D.4 of the Project, Shanghai shall make available to each of Jinshan and Fengxian part of the proceeds of the Loan, and shall cause each of Jinshan and Fengxian to re-lend to its Respective Sewerage Companies a portion of the Loan proceeds so made available to it, pursuant to a Subsidiary Loan Agreement acceptable to the Bank, and under terms and conditions satisfactory to the Bank which shall include, without limitation, the following:

- (a) (i) The principal amount so re-lent: (A) by Jinshan to Jinshan OOC shall be the amount in Dollars (on the date, or respective dates, of withdrawal from the Loan Account or payment from the Special Account) of the value of the currency or currencies so withdrawn, or paid, on account of expenditures under Categories (1)(b) and (2)(b); (B) by Jinshan to Fengjing WPC shall be the amount in Dollars (on the date, or respective dates, of withdrawal from the Loan Account or payment from the Special Account) of the value of the currency or currencies so withdrawn, or paid, on account of expenditures under Categories (1)(c) and (2)(c); and (C) by Fengxian to Nanpai SDC shall be the amount in Dollars (on the date, or respective dates, of

withdrawal from the Loan Account or payment from the Special Account) of the value of the currency or currencies so withdrawn, or paid, on account of expenditures under Categories (1)(d) and (2)(d);

- (ii) Each Participating District shall recover from its Respective Sewerage Companies, the principal amount so made available, together with an amount equal to one percent (1%) of such principal amount, over a period of fifteen (15) years inclusive of a grace period of five (5) years;
- (iii) Each Participating District shall charge interest on such principal amount, withdrawn and outstanding from time to time at a rate equal to the rate of interest applicable from time to time to the Loan pursuant to Section 2.06 of the Loan Agreement; and
- (iv) Each Participating District shall charge a commitment charge on such principal amount, not withdrawn from time to time at a rate equal to three fourths of one percent (3/4 of 1%) per annum.

(b) Each Respective Sewerage Company shall undertake to: (i) carry out its Respective Parts of the Project with due diligence and efficiency and in accordance with appropriate management, financial, engineering and public utility practices and social and environmental standards acceptable to the Bank, and provide, promptly as needed, the funds, facilities and other resources required for the purpose; and (ii) without limitation on the foregoing, take all measures necessary to ensure that its Respective Parts of the Project shall be implemented in accordance with its Respective Resettlement Action Plan and with the Environmental Management Plan.

(c) Each Respective Sewerage Company shall undertake to procure the goods, works and consultants' services for its Respective Parts of the Project and to be financed out of the proceeds of the Loan in accordance with the provisions of Schedule 1 to this Agreement, and utilize such goods, works and consultants' services exclusively in the carrying out of its Respective Parts of the Project.

(d) Each Respective Sewerage Company shall undertake to enable its respective Participating District, Shanghai and the Bank to inspect such goods and the sites and works included in its Respective Parts of the Project, the operation thereof, and any relevant records and documents.

(e) Each Respective Sewerage Company shall undertake to take out and maintain with responsible insurers such insurance, against such risks and in such amounts, as shall be consistent with sound business practice, including, without limitation, such insurance to cover hazards incident to the acquisition, transportation and delivery of goods financed out of the proceeds of the Loan to the place of use or installation, any indemnity

thereunder to be made payable in a currency freely usable by said Sewerage Company to replace or repair such goods.

- (f) Each Respective Sewerage Company shall undertake to:
 - (i) maintain records and accounts adequate to reflect in accordance with sound accounting practices its operations and financial condition;
 - (ii) have its financial statements (balance sheets, statements of income and expenses and related statements) for each fiscal year audited, in accordance with appropriate auditing principles consistently applied, by independent auditors acceptable to the Bank; and
 - (iii) furnish to the Bank, to Shanghai and to its respective Participating District, as soon as available, but in any case not later than six (6) months after the end of each such year certified copies of said financial statements and accounts for such year as so audited; the report of such audit by said auditors in such scope and detail as the Bank, Shanghai or the respective Participating District shall have reasonably requested; and all such other information concerning said records, accounts and financial statements, as well as the audit thereof, as the Bank, Shanghai or the respective Participating District shall reasonably request.

(g) Each Respective Sewerage Company shall undertake to produce for each fiscal year, commencing in 2004, total revenues equivalent to not less than the sum of:

- (i) its total operating expenses, including for maintenance, and including depreciation; and
- (ii) the amount by which debt service requirements exceed the provision for depreciation.

(h) Each Respective Sewerage Company shall undertake to:

- (i) review by September 30 in each fiscal year commencing in 2004, on the basis of forecasts prepared in a manner satisfactory to the Bank, whether it would meet the requirements set forth in subparagraph (g) above, in respect of such year and the next following fiscal year, and furnish to the Bank, Shanghai and its respective Participating District the results of such review upon its completion; and

- (ii) if any such review shows that it would not meet the requirements set forth in subparagraph (g) above for the fiscal years covered by such review, promptly take all necessary measures (including, without limitation, adjustments of the structure or levels of its tariffs) in order to meet such requirements.

(i) Each Respective Sewerage Company shall undertake not to incur any debt unless a reasonable forecast of its revenues and expenditures shows that its estimated net revenues for each fiscal year during the term of the debt to be incurred shall be at least 1.3 times its estimated debt service requirements in such year on all of its debt including the debt to be incurred.

(j) Each Respective Sewerage Company shall undertake to:

- (i) maintain policies and procedures adequate to enable it to monitor and evaluate on an ongoing basis, in accordance with indicators satisfactory to the Bank and to Shanghai the carrying out of its Respective Parts of the Project and the achievement of the objectives thereof; and
- (ii) prepare, under terms of reference satisfactory to the Bank, to Shanghai and its respective Participating District, and submit to the Project Office semi-annual reports integrating the results of the monitoring and evaluation activities performed pursuant to clause (i) of this subparagraph (j) on the progress achieved in the carrying out of its Respective Parts of the Project during the period preceding the date of each such report.

10. Shanghai shall cause the Participating Districts to: (a) exercise their rights under the Subsidiary Loan Agreements with their Respective Sewerage Companies in such manner as to protect the interests of the Borrower, the Bank, Shanghai and said Participating Districts, and to accomplish the purposes of the Loan; and (b) except as the Bank and Shanghai shall otherwise agree, not assign, amend, abrogate or waive their respective Subsidiary Loan Agreements or any provision thereof.

11. For purposes of paragraphs 6 and 9 of this Schedule:

(a) The term “total revenues” means the sum of total operating revenues and net non-operating income.

(b) The term “total operating revenues” means revenues from all sources related to operations.

(c) The term “total operating expenses” means:

- (i) in respect of SMSC, all expenses related to operations, including administration, adequate maintenance, taxes and payments in lieu of taxes, but excluding interest and other charges on debt; and
- (ii) in respect of any Respective Sewerage Company, all expenses related to operations, including administration, adequate maintenance, taxes and payments in lieu of taxes, and provision for depreciation on a straight line basis at a rate of not less than 3.3% per annum of the average current gross value of the fixed assets in operation of said Respective Sewerage Company, or other basis acceptable to the Bank, but excluding interest and other charges on debt.

(d) The average current gross value of the Project Company' fixed assets in operation of SMSC, or of any Respective Sewerage Company, as the case may be, shall be calculated as one half of the sum of the gross value of its 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.

(e) 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.

(f) The term "debt" means any indebtedness of SMSC or any of the Respective Sewerage Company maturing by its terms more than one (1) year after the date on which it is originally incurred.

(g) Debt shall be deemed to be incurred:

- (i) 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
- (ii) under a guarantee agreement, on the date the agreement providing for such guarantee has been entered into.

(h) The term "net revenues" means the difference between:

- (i) the sum of revenues from all sources related to operations and net non-operating income, and
- (ii) 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.

- (i) The term “net non-operating income” means the difference between:
 - (i) revenues from all sources other than those related to operations; and
 - (ii) expenses, including taxes and payments in lieu of taxes, incurred in the generation of revenues in clause (i) above.

(j) 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.

(k) 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 (12) months, including accounts receivable, marketable securities, inventories and pre-paid expenses properly chargeable to operating expenses within the next fiscal year.

(l) 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 (12) months, including accounts payable, customer advances, debt service requirements, taxes and payments in lieu of taxes, and dividends.

(m) The term “capital expenditures” means all expenditures incurred on account of fixed assets, including interest charged to construction related to operations; and the term “average capital expenditures” in respect of any fiscal year means the average of capital expenditures incurred or expected to be incurred for that year, the previous fiscal year and the next following fiscal year.

(n) The term “reasonable forecast” means a forecast prepared by SMSC or any of the Respective Sewerage Company, as the case may be, not earlier than twelve months prior to the incurrence of the debt in question, which both the Bank and said Company accept as reasonable and as to which the Bank has notified said Company 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 said Company.

(o) Whenever, for the purposes of this Schedule, it shall be necessary to value, in terms of the currency of the Borrower, 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.

12. Shanghai shall: (a) by no later than December 31, 2005, complete a study on the Uper Huangpu Catchment and water modeling under terms of reference acceptable to the

Bank; and (b) thereafter provide the report of such study and the recommendations to the Bank for its review and comment.

13. Shanghai shall: (a) by no later than December 31, 2005, complete a study under terms of reference acceptable to the Bank, on measures to improve air quality in Shanghai; and (b) thereafter provide the report of such study and the recommendations developed in such study to the Bank for its review and comment.

14. Shanghai shall:

(a) by no later than December 31, 2005, develop and adopt an administrative framework and implementing regulations for the execution of service or management contracts and/or concessions for wastewater services; and

(b) by no later than June 30, 2006, execute, or cause to be executed, a contract for private sector participation in the design, construction, operation and maintenance of a wastewater treatment facility of a reasonable capacity for the Shanghai metropolitan area.

15. Shanghai shall:

(a) maintain policies and procedures adequate to enable it to monitor and evaluate on an ongoing basis, in accordance with indicators satisfactory 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 January 31 and July 31 of each year, commencing in 2004, a semi-annual report, integrating the results of the monitoring and evaluation activities performed pursuant to sub-paragraph (a) of this paragraph 15 and incorporating the reports prepared and submitted by, or on behalf of, SMSC, Chengtou, the Participating Districts and the Respective Sewerage Companies in accordance with the provisions of paragraphs 6 and 9 of this Schedule; each such report to: (i) set out physical progress in the implementation of the Project, both cumulatively, and in respect of the preceding calendar semester, and explain variances between the actual and planned Project implementation; and (ii) set forth the status of procurement under the Project as at the end of the period covered by said report;

(c) prepare, under terms of reference satisfactory to the Bank and furnish to the Bank on or about September 30, 2006, a mid-term report on the progress achieved in the carrying out of the Project during the period preceding such 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

(d) review with the Bank by December 31, 2006, or such later date as the Bank shall request, the mid-term report referred to in subparagraph (c) of this paragraph 15, 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's views on the matter.