

CONFORMED COPY

LOAN NUMBER 2774 EC

(Second Guayaquil and Guayas Province Water Supply Project)

between

INTERNATIONAL BANK FOR RECONSTRUCTION
AND DEVELOPMENT

and

EMPRESA PROVINCIAL DE AGUA POTABLE DEL GUAYAS

Dated June 17, 1991

LOAN NUMBER 2774 EC

PROJECT AGREEMENT

AGREEMENT, dated June 17, 1991, between INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT (the Bank) and EMPRESA PROVINCIAL DE AGUA POTABLE DEL GUAYAS (hereinafter called EPAP-G).

WHEREAS (A) by a loan agreement of September 26, 1987 between the Empresa Municipal de Agua Potable de Guayaquil (hereinafter called EMAP-G) and the Bank (hereinafter called the Loan Agreement), the Bank made a loan (hereinafter called the Loan) to EMAP-G in an amount in various currencies equivalent to thirty one million dollars (\$31,000,000), on the terms and conditions set forth in the Loan Agreement;

(B) by a loan assumption agreement of even date herewith between the Republic of Ecuador (hereinafter called the Republic) and the Bank (hereinafter called the Loan Assumption Agreement), the Republic has agreed to assume all of the covenants, agreements and obligations of EMAP-G as Borrower (as distinguished from EMAP-G's role as Project executing agency) contained or referred to in the Loan Agreement;

(C) by a subsidiary arrangement to be entered into between the Republic and EPAP-G, the proceeds of the loan provided for under the Loan Agreement will be onlent to EPAP-G on the terms and conditions set forth in said subsidiary arrangement; and

WHEREAS EPAP-G, in consideration of the Bank's entering into the Loan Assumption Agreement with the Republic, has agreed to undertake the obligations set forth in this Agreement and thus replace EMAP-G, whose functions, assets and liabilities EPAP-G assumed pursuant to Law No. 38 (as defined in the Preamble to the Loan Assumption Agreement), as Project executing agency;

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 Loan Assumption Agreement, the Preamble to this Agreement and the General Conditions (as so defined) have the respective meanings therein set forth and the following additional terms have the following meanings:

(a) "Project Implementation Unit" means the unit referred to in Section 2.02 of this Agreement; and

(b) "Financial Rehabilitation Program" means EPAP-G's action program, referred to in Section 4.03 of this Agreement, to improve its financial performance.

ARTICLE II

Execution of the Project

Section 2.01. (a) EPAP-G declares its commitment to the objectives of the Project as set forth in Schedule 2 to the Loan 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, or cause to be provided, promptly as needed, the funds, facilities, services and other resources required for the Project.

(b) EPAP-G shall:

- (i) carry out the technical assistance and training program and the studies included under Parts B.1 and C of the Project, respectively, under terms of reference satisfactory to the Bank;
- (ii) promptly upon their completion, furnish to the Bank, for its comments, the results and recommendations of each of the studies included under the Project; and
- (iii) not later than December 31, 1992, complete the study referred to in Part C.3 of the Project, such study to include a program to implement its recommendations.

(c) EPAP-G shall:

- (i) establish eligibility criteria and financial conditions for the Credit Program, satisfactory to the Bank, which shall include: (A) a down payment of not less than 5%; (B) an amortization period not exceeding 5 years; and (C) a variable interest rate and other financial terms on each loan, satisfactory to the Bank, that will allow EPAP-G to recover the principal amount and all other costs of EPAP-G in real terms; and

- (ii) establish a revolving fund in terms satisfactory to the Bank where the amount paid to EPAP-G under all loans made under the Credit Program will be deposited and shall utilize the proceeds of such fund solely for purposes of making new loans for residential water connections.

(d) EPAP-G shall provide the Project Implementation Unit with adequate resources to carry out its functions.

Section 2.02. For purposes of carrying out the Project, EPAP-G shall establish and maintain, until the completion report referred to in Section 9.07 (c) of the General Conditions has been furnished to the Bank, a Project Implementation Unit with staffing, organization and functions satisfactory to the Bank.

Section 2.03. EPAP-G shall, no later than December 31, 1991, enter into contractual arrangements, under terms and conditions satisfactory to the Bank, with an established entity or entities acceptable to the Bank (such as a water company or consulting firm) for assisting EPAP-G in the carrying out of Part B.1 of the Project. Except as the Bank shall otherwise agree, EPAP-G shall not take or concur in any action which would have the effect of amending, abrogating, assigning or waiving such contractual arrangements or any provision thereof.

Section 2.04. (a) Except as the Bank shall otherwise agree, procurement of the goods, works and consultants' services required for the Project and to be financed out of the proceeds of the Loan shall be governed by the provisions of Schedule 4 to the Loan Agreement.

(b) As part of the foregoing, EPAP-G shall, not later than December 31, 1991, employ the consultants required for the study included under Part C.3 of the Project.

Section 2.05. EPAP-G shall carry out the obligations set forth in Sections 9.04, 9.05, 9.06, 9.07, 9.08 and 9.09 of the General Conditions (relating to insurance, use of goods and services, plans and schedules, records and reports, maintenance and land acquisition, respectively) in respect of the Project. As part of its obligations under Section 9.07 (a) (iii) of the General Conditions, and without limiting any of its other obligations under this Agreement, EPAP-G shall furnish to the Bank every six months, from the date this Agreement becomes effective pursuant to Section 5.01 of this Agreement and until the report referred to in Section 9.07 (c) of the General Conditions is furnished to the Bank, reports in such form as the Bank shall reasonably request regarding the status and progress of Project execution.

Section 2.06. EPAP-G shall enter into, and duly perform all its obligations under, the subsidiary arrangement referred to in Section 5.01 (b) of the Loan Assumption Agreement. Except as the Bank shall otherwise agree, EPAP-G shall not take or concur in any action which would have the effect of amending, abrogating, assigning or waiving such subsidiary arrangement or any provision thereof.

Section 2.07. (a) EPAP-G shall, at the request of the Bank, or also in combination with the furnishing of reports referred to in Section 2.05 of this Agreement, exchange views with the Bank with regard to progress of the Project, the performance of its obligations under this Agreement and under the subsidiary arrangement referred to in Section 5.01 (b) of the Loan Assumption Agreement, and other matters relating to the purposes of the Loan.

(b) EPAP-G 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 the Loan, or the performance by EPAP-G of its obligations under this Agreement and under the subsidiary arrangement referred to in Section 5.01 (b) of

the Loan Assumption Agreement.

Section 2.08. EPAP-G shall, not later than December 31, 1992, complete the installation of the Main transmission pipes in a manner satisfactory to the Bank.

ARTICLE III

Management and Operations of EPAP-G

Section 3.01. EPAP-G 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.

Section 3.02. EPAP-G 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, financial and public utility practices.

Section 3.03. EPAP-G shall at all times maintain its existence and right to carry on its operations and shall, except as the Bank shall otherwise agree, take all necessary steps that are required to acquire, maintain and renew all rights, powers, privileges and franchises which are necessary or useful in the conduct of its business.

Section 3.04. EPAP-G shall take out and maintain with responsible insurers, or make other provision satisfactory to the Bank for, insurance against such risks and in such amounts as shall be consistent with appropriate practice.

Section 3.05. Except as the Bank and EPAP-G shall otherwise agree, EPAP-G shall not sell, lease, transfer or otherwise dispose of its property or assets which shall be required for the efficient operation of its business, including the Project.

ARTICLE IV

Financial Covenants

Section 4.01. (a) EPAP-G shall maintain separate records and accounts adequate to reflect, in accordance with consistently maintained sound accounting practices, its operations and financial condition, including separate records and accounts to reflect the operations, resources and expenditures in respect of the Project.

(b) EPAP-G shall:

- (i) have its records and accounts referred to in paragraph (a) of this Section and financial statements (balance sheets, statements of income and expenses and related statements) for each fiscal year audited, in accordance with appropriate auditing principles consistently applied, by independent private auditors acceptable to the Bank acting under terms of reference satisfactory 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.

Section 4.02. (a) Except as the Bank shall otherwise agree, EPAP-G shall produce, for each of its fiscal years after its fiscal year ending December 31, 1991, total revenues from internal sources equivalent to not less than the sum of its: (i) operating expenses; (ii) increase in working capital; (iii) debt service requirements; and (iv) until completion of the Project, amounts equivalent to the following percentages of the annual expenditures for the Project: 5% in 1992, 15% in 1993, 20% in 1994, 25% in 1995 and 30% thereafter.

(b) Before September 30 in each of its fiscal years, EPAP-G shall, on the basis of forecasts prepared by EPAP-G 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 three following fiscal years and shall furnish to the Bank a copy of such review upon its completion.

(c) If any such review shows that EPAP-G would not meet the requirements set forth in paragraph (a) for EPAP-G's fiscal years covered by such review, EPAP-G shall promptly take all necessary measures (including, without limitation, adjustments of the structure or levels of its tariffs) in order to meet such requirements for at least the current and the next following fiscal years.

(d) For purposes of this Section:

- (i) The term "total revenues from internal sources" means the sum of total operating revenues and net non-operating income.
- (ii) The term "total operating revenues" means revenues from all sources related to operations.
- (iii) The term "net nonoperating 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.
- (iv) The term "operating expenses" means all expenses related to operations, including administration, adequate maintenance, and taxes and payment in lieu of taxes, excluding provisions for depreciation and interest and other charges on debt.
- (v) The term "working capital" means the difference between current assets excluding cash and current liabilities at the end of each fiscal year.
- (vi) 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 all amounts due to EPAP-G under the Credit Program, accounts receivable, marketable securities, inventories and prepaid expenses properly chargeable to operating expenses within the next fiscal year.
- (vii) 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.
- (viii) 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.

- (ix) Whenever for the purposes of this Section it shall be necessary to value, in terms of the currency of the Guarantor, debt payable in another currency, such valuation shall be made on the basis of the prevailing lawful rate of exchange at which such other currency is, at the time of such valuation, obtainable for the purposes of servicing such debt, or in the absence of such rate, on the basis of a rate of exchange acceptable to the Bank.

Section 4.03. (a) No later than June 30, 1991, EPAP-G shall cause the Financial Rehabilitation Program to be prepared by combining the results of work performed for this purpose by consultants and by various study commissions, and shall immediately thereafter begin and continue carrying out the Financial Rehabilitation Program in a manner satisfactory to the Bank and according to a timetable satisfactory to the Bank. The Financial Rehabilitation Program shall include, inter alia, a plan and timetable for modifying EPAP-G's tariff structure, for reducing unaccounted-for water and for improving metering, billing and collection practices, all so as to improve revenues for EPAP-G. Such plan may include measures aimed at contracting with a private firm to carry out commercial activities, such as billing and collection, on behalf of EPAP-G in certain areas of Guayaquil or Guayas Province.

(b) Until its completion and not later than September 30 of each year, EPAP-G shall update the Financial Rehabilitation Program, including performance and financial targets satisfactory to the Bank which are consistent, inter alia, with the targets referred to in Section 4.02 (a) of this Agreement.

(c) Without limitation to the foregoing, EPAP-G and the Bank shall, from time to time, review the financial condition and operational performance of EPAP-G. To that effect, EPAP-G shall, before September 30 of each year and at all other times as the Bank shall reasonably request, provide all information necessary or appropriate for the purpose of conducting such reviews.

Section 4.04. Before September 30, 1991, EPAP-G shall hire consultants to conduct an inventory and revaluation of EPAP-G's assets, and EPAP-G shall cause such inventory and revaluation to be completed no later than April 30, 1992.

Section 4.05. EPAP-G shall cause a consultant to develop an integrated general and cost accounting, budgeting and long-term financial planning system, satisfactory to the Bank, which shall be operational by no later than October 31, 1991. EPAP-G shall have all its accounting current (or within no more than one month of being current) by no later than January 31, 1992.

Section 4.06. (a) Before August 30, 1991, EPAP-G shall furnish to the Bank the audit reports and certified copies of financial statements for calendar year 1988 and through August 3 of calendar year 1989 which EPAP-G should have furnished to the Bank pursuant to Section 5.01 (b) (ii) of the Loan Agreement (as such Section read prior to the Loan Agreement's amendment pursuant to Article III of the Loan Assumption Agreement).

(b) Also before August 30, 1991, EPAP-G shall furnish to the Bank an audit report and a certified copy of its financial statements for that part of calendar year 1989 beginning on August 3 and for calendar year 1990, as if Section 4.01 (b) (ii) of this Agreement had been in effect for such periods.

ARTICLE V

Effective Date; Termination;

Cancellation and Suspension

Section 5.01. This Agreement shall come into force and effect on the date upon which the Loan Assumption Agreement becomes effective.

Section 5.02. This Agreement and all obligations of the Bank and of EPAP-G thereunder shall terminate on the date on which the Loan Agreement shall terminate in accordance with its terms, and the Bank shall promptly notify EPAP-G thereof.

Section 5.03. All the provisions of this Agreement shall continue in full force and effect notwithstanding any cancellation or suspension under the General Conditions.

ARTICLE VI

Miscellaneous Provisions

Section 6.01. 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, telegram, cable, telex or radiogram 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. The addresses so specified are:

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:

197688 (ITT),
248423 (RCA) or
64145 (WUI)

For EPAP-G:

Empresa Provincial de Agua Potable del Guayas
Clemente Ballen 211
Casilla 5253
Guayaquil, Ecuador

Telex:

3398 EPAPGY-ED

Section 6.02. Any action required or permitted to be taken, and any document required or permitted to be executed, under this Agreement on behalf of EPAP-G may be taken or executed by its Director Ejecutivo or such other person or persons as its Director Ejecutivo shall designate in writing, and EPAP-G shall furnish to the Bank sufficient evidence of the authority and the authenticated specimen signature of each such person.

Section 6.03. All actions taken, rights acquired or obligations incurred under the Loan Agreement by EMAP-G as Project executing agency (as distinguished from its former role as Borrower) shall be valid and binding on EPAP-G as though EPAP-G had been EMAP-G and the coming into effect of this Agreement shall not affect the consequences of any action taken or omitted to be taken by the Bank or EMAP-G as Project executing agency (as distinguished from its former role as Borrower) under the Loan Agreement.

Section 6.04. 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 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/ Shahid Husain
Regional Vice President
Latin America and the Caribbean

EMPRESA PROVINCIAL DE AGUA POTABLE
DEL GUAYAS

By /s/ Galo Betancourt S nchez
Authorized Representative

