

CONFORMED COPY

LOAN NUMBER 4657 TU

Loan Agreement

**(Second Programmatic Financial and Public
Sector Special Adjustment Loan)**

between

REPUBLIC OF TURKEY

and

**INTERNATIONAL BANK FOR RECONSTRUCTION
AND DEVELOPMENT**

Dated April 24, 2002

LOAN NUMBER 4657 TU

LOAN AGREEMENT

AGREEMENT, dated April 24, 2002, between REPUBLIC OF TURKEY (the

Borrower) and INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT (the Bank).

WHEREAS (A) pursuant to the loans (Loan No. 4632 TU and Loan No. 4633 TU) provided to the Borrower under the loan agreements, dated July 12, 2001, the Bank has provided assistance to the Borrower in support of the first phase of the Borrower's program of actions, objectives and policies designed to achieve structural adjustment of the Borrower's financial and public sectors (the Program), as such program was described in the letter, dated June 18, 2001, from the Borrower to the Bank;

(B) the Bank has received a letter, dated March 19, 2002, from the Borrower: (i) describing its macro-economic framework and the Program, as revised since the date of the letter referred to in (A) above, which Program consists of actions taken under the first phase referred to in (A) above, and actions and policies that the Borrower has taken or intends to take and adopt in the near future (the Second Phase of the Program); (ii) declaring the Borrower's commitment to the execution of the Program; and (iii) requesting assistance from the Bank in support of the Program during the execution thereof;

(C) the Borrower has also requested the Bank to provide additional assistance in support of the Second Phase of the Program and by an agreement of even date herewith between the Borrower and the Bank (the Second PFPSAL Loan Agreement), the Bank is agreeing to provide such assistance in an amount equal to five hundred fifty million Dollars (\$550,000,000) (Second PFPSAL Loan); and

(D) on the basis, inter alia, of the foregoing, the Bank has decided in support of the Second Phase of the Program to provide such assistance to the Borrower by making the Loan in three tranches as hereinafter provided;

NOW THEREFORE the parties hereto hereby agree as follows:

ARTICLE I

General Conditions; Definitions

Section 1.01. The "General Conditions Applicable to Loan and Guarantee Agreements for Single Currency Loans" of the Bank, dated May 30, 1995 (as amended through October 6, 1999), with the modifications set forth below (the General Conditions) constitute an integral part of this Agreement:

(a) Section 2.01, paragraph 18, is modified to read: "'Project' means the second phase of the program, referred to in the Preamble to the Loan Agreement, in support of which the Loan is made.";

(b) Section 4.01 is modified to read: "Except as the Bank and the Borrower shall otherwise agree, withdrawals from the Loan Account shall be made in the currency of the deposit account specified in Section 2.02 of the Loan Agreement.";

(c) Section 5.01 is modified to read: "The Borrower shall be entitled to withdraw the proceeds of the Loan from the Loan Account in accordance with the provisions of the Loan Agreement and of these General Conditions";

(d) the last sentence of Section 5.03 is deleted;

(e) Section 9.07 (c) shall be modified to read:

“(c) Not later than six months after the Closing Date or such later date as may be agreed for this purpose between the Borrower and the Bank, the Borrower shall prepare and furnish to the Bank a report, of such scope and in such detail as the Bank shall reasonably request, on the execution of the program referred to in the Preamble to the Loan Agreement, the performance by the Borrower and the Bank of their respective obligations under the Loan Agreement and the accomplishment of the purposes of the Loan.”; and

(f) Section 9.05 is deleted and Sections 9.06, 9.07 (as modified above), 9.08 and 9.09 are renumbered, respectively, Sections 9.05, 9.06, 9.07 and 9.08.

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

(a) “BRSA” means the Bank Regulatory and Supervisory Agency of the Borrower, or any successor thereto acceptable to the Bank;

(b) “Central Bank” or “CBT” means the Central Bank of the Borrower;

(c) “Deposit Account” means the account referred to in Section 2.02 (b) of this Agreement;

(d) “GFS” means the government financial statistics published by the International Monetary Fund;

(e) “MOF” means the Ministry of Finance of the Borrower;

(f) “PIP” means the Borrower’s annual Public Investment Program;

(g) “SDIF” means the Savings and Deposit Insurance Fund of the Borrower, or any successor thereto acceptable to the Bank;

(h) “SEEs” means State Economic Enterprises;

(i) “SPO” means the State Planning Organization of the Borrower;

(j) “TCA” means the Turkish Court of Accounts of the Borrower; and

(k) “Treasury” means the Undersecretariat of Treasury of the Borrower.

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 eight hundred million Dollars (\$800,000,000).

Section 2.02. (a) Subject to the provisions of paragraphs (b), (c) and (d) of this Section, the Borrower shall be entitled to withdraw the proceeds of the Loan from the Loan Account in support of the Program.

(b) The Borrower shall open, prior to furnishing to the Bank the request for withdrawal from the Loan Account, and thereafter maintain in its Central Bank, a deposit account in Dollars on terms and conditions satisfactory to the Bank. All withdrawals from the Loan Account shall be deposited by the Bank into the Deposit Account.

(c) The Borrower undertakes that the proceeds of the Loan shall not be used to finance expenditures excluded pursuant to the provisions of Schedule 1 to this Agreement. If the Bank shall have determined at any time that any proceeds of the Loan shall have been used to make a payment for an expenditure so excluded, the Borrower shall, promptly upon notice from the Bank: (i) deposit into the Deposit Account an amount equal to the amount of said payment; or (ii) if the Bank shall so request, refund such amount to the Bank. Amounts refunded to the Bank upon such request shall be credited to the Loan Account for cancellation.

(d) No withdrawals shall be made from the Loan Account:

(i) after the aggregate of the proceeds of the Loan withdrawn from the Loan Account shall have reached the equivalent of \$266,000,000, unless the Bank shall be satisfied, after an exchange of views as described in Section 3.01 of this Agreement based on evidence satisfactory to the Bank:

(A) with the progress achieved by the Borrower in the carrying out of the Program;

(B) that the macro-economic policy framework of the Borrower is satisfactory, as measured on the basis of indicators agreed between the Borrower and the Bank; and

(C) that the actions described in Section I of Schedule 3 to this Agreement have been taken; and

(ii) after the aggregate of the proceeds of the Loan withdrawn from the Loan Account shall have reached the equivalent of \$533,000,000, unless the Bank shall be satisfied, after an exchange of views as described in Section 3.01 of this Agreement based on evidence satisfactory to the Bank:

(A) with the progress achieved by the Borrower in the carrying out of the Program;

(B) that the macro-economic policy framework of the Borrower is satisfactory, as measured on the basis of indicators agreed

between the Borrower and the Bank; and

- (C) that the actions described in Section II of Schedule 3 to this Agreement have been taken.

Section 2.03. The Closing Date shall be December 31, 2002, or such later date as the Bank shall establish. The Bank shall promptly notify the Borrower of such later date.

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

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

Section 2.06. (a) The Borrower shall pay interest on the principal amount of the Loan withdrawn and outstanding from time to time, at a rate for each Interest Period equal to LIBOR Base Rate plus 4 (four) percentage points.

(b) For the purposes of this Section:

- (i) "Interest Period" means the initial period from and including the date of this Agreement to, but excluding, the first Interest Payment Date occurring thereafter, and after the initial period, each period from and including an Interest Payment Date to, but excluding the next following Interest Payment Date.
- (ii) "Interest Payment Date" means any date specified in Section 2.07 of this Agreement.
- (iii) "LIBOR Base Rate" means, for each Interest Period, the London interbank offered rate for six-month deposits in 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.

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

(d) Whenever, in light of changes in market practice affecting the determination of the interest rates referred to in this Section 2.06, the Bank determines that it is in the interest of its borrowers as a whole and of the Bank to apply a basis for determining the interest rates applicable to the Loan other than as provided in said Section, the Bank may modify the basis for determining the interest rates applicable to the Loan upon not less than six (6) months' notice to the Borrower of the new basis. Such new 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 2.07. Interest and other charges shall be payable semiannually in arrears on April 15 and October 15 in each year.

Section 2.08. The Borrower shall repay the principal amount of the Loan in accordance with the amortization schedule set forth in Schedule 2 to this Agreement.

ARTICLE III

Particular Covenants

Section 3.01. (a) The Borrower and the Bank shall from time to time, at the request of either party, exchange views on the progress achieved in carrying out the Program and the actions specified in Schedule 3 to this Agreement.

(b) Prior to each such exchange of views, the Borrower shall furnish to the Bank for its review and comment a report on the progress achieved in carrying out the Program, in such detail as the Bank shall reasonably request.

(c) Without limitation upon the provisions of paragraph (a) of this Section, the Borrower shall exchange views with the Bank on any proposed action to be taken after the disbursement of the Loan which would have the effect of materially reversing the objectives of the Program, or any action taken under the Program, including any action specified in Schedule 3 to this Agreement.

Section 3.02. Upon the Bank's request, the Borrower shall:

(a) have the Deposit Account audited in accordance with appropriate auditing principles consistently applied, by independent auditors acceptable to the Bank;

(b) furnish to the Bank as soon as available, but in any case not later than four months after the date of the Bank's request for such audit, a certified copy of the report of such audit by said auditors, of such scope and in such detail as the Bank shall have reasonably requested; and

(c) furnish to the Bank such other information concerning the Deposit Account and the audit thereof as the Bank shall have reasonably requested.

ARTICLE IV

Additional Event of Suspension

Section 4.01. Pursuant to Section 6.02 (p) of the General Conditions, the following additional event is specified, namely, that a situation has arisen which shall make it improbable that the Program, or a significant part thereof, will be carried out.

ARTICLE V

Effective Date; Termination

Section 5.01. The following events are specified as additional conditions to the effectiveness of the Loan Agreement within the meaning of Section 12.01(c) of the General Conditions:

(a) the macroeconomic policy framework of the Borrower is consistent with the objectives of the Program;

(b) all conditions precedent to the effectiveness of the Second PFPSAL Loan Agreement have been fulfilled, other than those related to the effectiveness of this Agreement; and

(c) the Borrower has submitted to Parliament draft legislation (i) to extend the coverage of TCA audits to the Parliament and Presidency; and (ii) for external audit of TCA itself.

Section 5.02. The date sixty (60) days after the date of this Agreement is hereby specified for the purposes of Section 12.04 of the General Conditions.

ARTICLE VI

Representative of the Borrower; Addresses

Section 6.01. The Undersecretary of Treasury of the Borrower is designated as representative of the Borrower for the purposes of Section 11.03 of the General Conditions.

Section 6.02. The following addresses are specified for the purposes of Section 11.01 of the General Conditions:

For the Borrower:

Basbakanlik
Hazine Mustesarligi
Inonu Bulvari
Emek - Ankara
Republic of Turkey
06510

Cable address:	Telex:	Facsimile:
HAZINE	44 232 HZM-TR	(312) 212-8550
Hazine, Ankara	44 404 HZM-TR	

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

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

REPUBLIC OF TURKEY

By /s/ Kemal Dervis

Authorized Representative

INTERNATIONAL BANK FOR
RECONSTRUCTION AND DEVELOPMENT

By /s/ Johannes Linn

Regional Vice President
Europe and Central Asia

SCHEDULE 1

Excluded Expenditures

For purposes of Section 2.02 (c) of this Agreement, the proceeds of the Loan shall not be used to finance any of the following expenditures:

1. expenditures in the currency of the Borrower or for goods or services supplied from the territory of the Borrower;
2. expenditures for goods or services supplied under a contract which any national or international financing institution or agency other than the Bank or the Association shall have financed or agreed to finance, or which the Bank or the Association shall have financed or agreed to finance under another loan or a credit;
3. expenditures for goods included in the following groups or subgroups of the Standard International Trade Classification, Revision 3 (SITC, Rev.3), published by the United Nations in Statistical Papers, Series M, No. 34/Rev.3 (1986) (the SITC), or any successor groups or subgroups under future revisions to the SITC, as designated by the Bank by notice to the Borrower:

<u>Group</u>	<u>Subgroup</u>	<u>Description of Items</u>
112	-	Alcoholic beverages
121	-	Tobacco, unmanufactured, tobacco refuse
122	-	Tobacco, manufactured (whether or not containing tobacco substitutes)
525	-	Radioactive and associated materials
667	-	Pearls, precious and semiprecious stones, unworked or worked
718	718.7	Nuclear reactors, and parts thereof; fuel elements (cartridges), non-irradiated, for nuclear reactors
728	728.43	Tobacco processing

897	897.3	machinery Jewelry of gold, silver or platinum group metals (except watches and watch cases) and goldsmiths' or silversmiths' wares (including set gems)
971	-	Gold, non-monetary (excluding gold ores and concentrates)

4. expenditures for goods intended for a military or paramilitary purpose or for luxury consumption;

5. expenditures for environmentally hazardous goods (for purposes of this paragraph the term "environmentally hazardous goods" means goods, the manufacture, use or import of which is prohibited under the laws of the Borrower or international agreements to which the Borrower is a party);

6. expenditures: (a) in the territories of any country which is not a member of the Bank or for goods procured in, or services supplied from, such territories; or (b) on account of any payment to persons or entities, or any import of goods, if such payment or import is prohibited by a decision of the United Nations Security Council taken under Chapter VII of the Charter of the United Nations; and

7. expenditures under a contract in respect of which the Bank determines that corrupt or fraudulent practices were engaged in by representatives of the Borrower or of a beneficiary of the Loan during the procurement or execution of such contract, without the Borrower having taken timely and appropriate action satisfactory to the Bank to remedy the situation.

SCHEDULE 2

Amortization Schedule

<u>Date Payment Due</u>	<u>Payment of Principal (Expressed in Dollars)*</u>
On each April 15 and October 15	
beginning October 15, 2005 through April 15, 2007	200,000,000

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

SCHEDULE 3

Actions Referred to in Section 2.02 (d) of this Agreement

Section I: Actions Referred to in Section 2.02 (d) (i) of this Agreement

I. Macroeconomic Framework

1. The Borrower has implemented a satisfactory macro-economic framework up to the time of the exchange of views referred to in Section 3.01 of this Agreement, including at least the first quarter of calendar year 2002, such macro-economic framework to be evaluated on the basis of the overall Program and with respect to domestic interest rates, inflation, maturity of new Government domestic borrowing, budget outcome and private capital inflows.

II. Financial Sector Reform

A. Regulatory Framework for Banking Activity

2. The Borrower has developed satisfactory detailed actions plans for banks with excess connected exposures to reach compliance with the new banking law limits, including proposals to address any remaining legal/tax hurdles to merger/de-mergers necessary for implementing such action plans.

B. Institutional Development of SDIF

3. SDIF has prepared, and its Board has approved, a satisfactory time-bound strategic plan with clearly assigned implementation responsibilities to: (i) put in place a more effective organizational structure, with clearly separated line responsibilities for bank resolution efforts, asset management efforts, administration of the blanket guarantee and the deposit insurance scheme, and supporting functions such as legal, human resources and information technology; (ii) set performance targets for the bank resolution and asset management functions; (iii) envisage the hiring of additional qualified staff to handle the high volume of non-performing loans and other problem assets to be transferred to the Collections Department for collection/workout; and (iv) build a centralized and high quality management information system that will allow SDIF senior management and the SDIF Board to monitor progress being made towards reaching agreed resolution and asset management/collection targets.

C. Problem Bank/Bank Failure Resolution

4. BRSA has issued satisfactory implementing regulations for the public support scheme for private bank recapitalization.

5. SDIF has carried out satisfactory implementation of the asset resolution strategy, including transfer of all remaining assets to a specific asset resolution entity or its own departments.

6. The Borrower has undertaken a satisfactory coordinated review of the improvements required in the legal framework for bankruptcy and collateral foreclosure and accelerated/more

efficient non-performing loan resolution.

D. State Bank Restructuring and Privatization

7. Halk and Ziraat have made satisfactory substantial progress towards unprofitable branch closures and excess staff reductions.

8. The Borrower, through its Treasury, has made all interest payments to Ziraat and Halk on government bonds necessary for elimination of short term liabilities on the books of Ziraat and Halk in cash during 2002, as per the agreement between the Treasury and the management of Ziraat and Halk.

III. Public Sector Reform

E. Structural Fiscal Policies

9. The Borrower has made satisfactory progress in the implementation of its medium-term strategy to improve the tax system.

10. The Borrower has made satisfactory progress in the implementation of its comprehensive public employment program.

F. Public Expenditure Management

11. The Borrower's MOF has issued a circular expanding the new GFS budget classification to all general government agencies.

12. The Borrower has adopted a satisfactory action plan for further improvements in the PIP beyond 2002.

G. Financial Accountability

13. The Borrower has enacted legislation to extend the coverage of TCA audits to the Parliament and Presidency, and TCA has implemented the proposal for external audit of TCA itself.

H. Public Liability Management

14. The Borrower has adopted regulations for the issuance of government guarantees in accordance with the public debt management law and for borrowing by SEEs.

I. Public Sector Governance

15. The Borrower has made satisfactory progress in the implementation of its national strategy to enhance transparency and good governance in the public sector.

Section II: Actions Referred to in Section 2.02 (d) (ii) of this Agreement

I. Macroeconomic Framework

1. The Borrower has implemented a satisfactory macro-economic framework up to the time of the exchange of views referred to in Section 3.01 of this Agreement, including at least the second quarter of calendar year 2002, such macro-economic framework to be evaluated on the basis of the overall Program and with respect to domestic interest rates, inflation, maturity of new Government domestic borrowing, budget outcome and private capital inflows.

II. Financial Sector Reform

A. Regulatory Framework for Banking Activity

2. The Borrower has made satisfactory progress in the implementation of the action plans for banks with excess connected exposures.

B. Problem Bank/Bank Failure Resolution

3. With respect to capital deficient banks, the Borrower has either implemented satisfactory capital restoration plans or implemented satisfactory SDIF resolution actions, including capital injections, interventions, mergers/closures for such banks.

4. The Borrower has completed the resolution of any banks taken over by SDIF in 2001, including Turk Ticaret and Tiris, subject to the final administrative court decision allowing for the resolution of these two banks.

C. State Bank Restructuring and Privatization

5. Halk and Ziraat have completed all necessary branch closures and excess staff reductions.

6. The Borrower, through its Treasury, has made all interest payments on government bonds necessary for elimination of short term liabilities on the books of Ziraat and Halk in cash during 2002, as per the agreement between the Treasury and the management of Ziraat and Halk, and adjusted for any major changes in the liability maturities in Ziraat and Halk.

7. The Borrower has completed the privatization (100 percent) of Vakif.

III. Public Sector Reform

D. Structural Fiscal Policies

8. The Borrower has made satisfactory progress in the implementation of its medium-term strategy to improve the tax system.

9. The Borrower has made satisfactory progress in the implementation of the comprehensive public employment program.

E. Public Expenditure Management

10. The Borrower has made satisfactory progress in the implementation of the GFS pilot program.

F. Financial Accountability

11. New accounting standards and chart of accounts for general government in compliance with GFS requirements have been published in the official gazette.

12. The Borrower has made satisfactory progress in implementing the new framework for public procurement, including the appointment of the Board for the Public Procurement Agency and enactment of amendments to the Public Procurement Law as agreed with the Bank.

13. The Borrower has submitted to Parliament the draft Law on Public Financial Management and Financial Control.

G. Public Sector Governance

14. The Borrower has made satisfactory progress in the preparation of a civil service reform strategy.

