

CONFORMED

LOAN NUMBER 4237 CHA

Loan Agreement

(Shandong Environment Project)

between

PEOPLE'S REPUBLIC OF CHINA

and

**INTERNATIONAL BANK FOR RECONSTRUCTION
AND DEVELOPMENT**

Dated February 4, 1998

LOAN NUMBER 4237 CHA

LOAN AGREEMENT

AGREEMENT, dated February 4, 1998, between PEOPLE'S REPUBLIC OF CHINA (the Borrower) and INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT (the Bank).

WHEREAS (A) the Borrower, having satisfied itself as to the feasibility and priority of the Project described in Schedule 2 to this Agreement, has requested the Bank to assist in the financing of the Project;

(B) Shandong Province (Shandong) shall carry out the Project, or cause the Project to be carried out, with the Borrower's assistance and, as part of such assistance, the Borrower will make available to Shandong the proceeds of the Loan as provided in this 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 and in the Project Agreement of even date herewith between the Bank and Shandong;

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, with the modification set forth below (the General Conditions) constitute an integral part of this Agreement:

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 terms, whenever used in this Agreement, have the following meanings:

(a) “Basic Documents” means the charters and business licenses referred to in paragraphs (f), (g), (ii) and (mm) of this Section.

(b) “Category” means a category of items to be financed out of the proceeds of the Loan as set forth in the table in paragraph 1 of Schedule 1 to this Agreement.

(c) “Environmental Action Plans”, means, collectively, the Shandong Environmental Assessment, the Xiaoqing Environmental Action Plan, the Main Polluter EAPs and the Sub-project EAPs.

(d) “Financial Agency Agreement” means the agreement to be entered into between Shandong and a financial institution pursuant to Part F.3 (b) of Schedule 2 to the Project Agreement.

(e) “Jinan” means Jinan Municipality in Shandong.

(f) “Jinan Drainage Company” means the Jinan Municipal Drainage Company, a state-owned company established and operating pursuant to its Charter approved on September 10, 1996 by Jinan Urban Construction Administration and to Business License No. 26435727-3, dated September 10, 1996, issued by Jinan Municipal Industrial and Commerce Administration Bureau.

(g) “Jinan Water Company” means the Jinan Municipal Water Supply Company, a state-owned company established and operating pursuant to its Charter dated December 1989 and to Business License No. 16315746-7, dated July 1, 1996 issued by Jinan Municipal Industrial and Commerce Administration Bureau.

(h) “Jinan Wastewater RAP” means Jinan’s ‘Wastewater Collection System Project Land Acquisition, Removal and Resettlement Action Plan (RAP)-1997.02,’ as received by the Bank on February 19, 1997, which is Jinan’s land acquisition, removal and resettlement plan for Part A.2 of the Project, and includes the procedures governing land acquisition, resettlement and compensation, as well as the reporting and monitoring arrangements to ensure compliance with the said, as the same may be revised from time to time in agreement with the Bank.

(i) “Jinan Water RAP” means Jinan’s “Yellow River Water Supply Project (Queshan Reservoir) Land Acquisition and Resettlement Action Plan” which is Jinan’s land acquisition, removal and resettlement plan for Part A.1 of the Project, dated March 1997, as received by the Bank on March 18, 1997, and includes the procedures governing land acquisition, resettlement and compensation, as well as the reporting and monitoring arrangements to ensure compliance with the said plan, as the same may be revised from time to time in agreement with the Bank.

(j) “Main Polluter EAP 1” means Shandong’s environmental action plan dated February 5, 1997 to reduce pollution caused by Jinan Iron and Steel Group Corporation, and which includes environmental mitigation measures and as well as the administrative and monitoring arrangements ensuring the implementation of said measures, as the same may be revised from time to time in agreement with the Bank

(k) “Main Polluter EAP 2” means the environmental action plan dated February 10, 1997 to reduce pollution caused by Qingzhou Paper Making Company, Ltd., and which includes environmental mitigation measures and as well as the administrative and monitoring arrangements ensuring the implementation of said measures, as the same may be revised from time to time in agreement with the Bank.

(l) “Main Polluter EAP 3” means the environmental action plan dated February 15, 1997 to reduce pollution caused by Shonguang Yongli Pulp Making Company, and which includes environmental mitigation measures and as well as the administrative and monitoring arrangements ensuring the implementation of said measures, as the same may be revised from time to time in agreement with the Bank.

(m) “Main Polluter EAPs” means collectively, Main Polluter EAP 1, Main Polluter EAP 2 and Main Polluter EAP 3.

(n) “Operational Regulations” means the manual referred to in Part F.2 (a) of Schedule 2 to the Project Agreement.

(o) “Participating Enterprise” means an enterprise to which Shandong proposes to make, or has made, a Sub-loan.

(p) “PPO” means Shandong’s provincial project office responsible for the overall coordination and supervision of Project implementation, as referred to in Part A.1 of Schedule 2 to the Project Agreement.

(q) “Project Agreement” means the agreement among the Bank and Shandong of even date herewith, as the same may be amended from time to time, and such term includes all schedules and agreements supplemental to the Project Agreement.

(r) “Project Municipalities” means, collectively, Jinan, Weihai and Yantai; and "Project Municipality" means any of the Project Municipalities.

(s) “Renminbi” means the currency of the Borrower.

(t) “Resettlement Action Plans” means, collectively, the Jinan Wastewater RAP, Jinan Water RAP, Weihai RAP, Yantai RAP and the Sub-project RAPs.

(u) “Respective Part of the Project” means, the part of the Project specified below:

- (i) for Shandong: Parts D, E.1(e) and (f), and E.2;
- (ii) for Jinan Water Company: Parts A.1 and E.1(a);
- (iii) for Jinan Drainage Company: Parts A.2 and E.1(b);
- (iv) for Weihai Company: Parts B and E.1 (c) and
- (v) for Yantai Company: Parts C and E.1. (d).

(v) “Respective RAP” means:

- (i) for Jinan Water Company: Jinan Wastewater RAP;
- (ii) for Jinan Drainage Company: Jinan Water RAP;
- (iii) for Weihai Company: Weihai RAP; and
- (iv) for Yantai Company: Yantai RAP.

(w) “SEPB” means Shandong’s bureau responsible for environmental protection.

(x) “SFB” means Shandong’s bureau responsible for finance.

(y) “Shandong” means Shandong Province, a political subdivision of the Borrower.

(z) “Shandong Environmental Assessment” means the environmental assessment for the Project dated December 17, 1996, and includes environmental mitigation measures and as well as the administrative and monitoring arrangements ensuring the implementation of said measures, as the same may be revised from time to time in agreement with the Bank.

(aa) “Special Account” means the account referred to in Section 2.02 (b) of this Agreement.

(bb) “Sub-loan” means a loan made, or proposed to be made by Shandong, out of the proceeds of the Loan, to a Participating Enterprise for a Sub-project.

(cc) “Sub-project” means a specific development project under Part D of the Project to be carried out by a Participating Enterprise utilizing the proceeds of a Sub-loan.

(dd) “Sub-project EAPs” means, collectively, the environmental action plans prepared pursuant to paragraph 2 (c) of Part B of Schedule 4 to the Project Agreement; and “Sub-project EPA” means, individually, any of the Sub-project EAPs.

(ee) “Sub-project RAPs” means, collectively, the resettlement action plans prepared pursuant to paragraph 2 (d) of Part B of Schedule 4 to the Project Agreement; and “Sub-project RAP” means, individually, any of the Sub-project RAPs.

(ff) “Subsidiary Loan Agreements” means, collectively, the agreements to be entered into between each Project Municipality and its Utility Company pursuant to Part D.1 of Schedule 2 to the Project Agreement, as the same may be amended from time to time, and such term includes any schedules to said agreements; and "Subsidiary Loan Agreement" means, individually, any of the Subsidiary Loan Agreements.

(gg) “Utility Company” means, in respect of:

(i) Jinan: the Jinan Water Company and the Jinan Drainage Company;

(ii) Weihai: the Weihai Company; and

(iii) Yantai: the Yantai Company.

(hh) “Weihai” means Weihai Municipality in Shandong.

(ii) “Weihai Company” means the Weihai Botong Heat and Power Company, Ltd., a state-owned limited liability company established and operating pursuant to its Charter dated September 1996 and to Business License No. 26636001-1, dated September 8, 1996, issued by Weihai Municipal Industrial and Commerce Administration Bureau.

(jj) “Weihai RAP” means Weihai’s ‘No.3 Heat and Power Plant Resettlement Action Plan - 6th draft October 1996’, as received by the Bank on February 19, 1997, which is Weihai’s land acquisition, removal and resettlement plan for Part B of the Project, and includes the procedures governing land acquisition, resettlement and compensation, as well as the reporting and monitoring arrangements to ensure compliance with the said plan, as the same may be revised from time to time in agreement with the Bank.

(kk) “Xiaoqing Environmental Action Plan” means the ‘Comprehensive Water Pollution Prevention and Control Plan for Xiaoqing River Basin’, dated September 1994, as approved by Shandong Provincial People’s Congress on June 14, 1995, and designed to address the significant point sources of pollution in the Xiaoqing River Basin, as the same may be revised from time to time in agreement with the Bank.

(ll) “Yantai” means Yantai Municipality in Shandong.

(mm) “Yantai Company” means the Yantai Heat Supply Company, a state-owned limited liability company established and operating pursuant to its Charter approved on September 11, 1996, by Yantai Municipal People’s Government and to Business License No. 26564401-2, dated January 16, 1997, issued by Municipal Industrial and Commerce Administration Bureau.

(nn) “Yantai RAP” means Yantai’s ‘Demonstration Project of Yantai 500 Heating Network Resettlement Action Plan - September 1996 Revision’, as received by the Bank on February 17, 1997, which is Yantai’s land acquisition, removal and resettlement plan for Part C of the Project, and includes the procedures governing land acquisition, resettlement and compensation, as well as the reporting and monitoring arrangements to ensure compliance with the said plan, as the same may be revised from time to time in agreement with the Bank.

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 ninety five million Dollars (\$95,000,000).

Section 2.02. (a) The amount of the Loan may be withdrawn from the Loan Account in accordance with the provisions of Schedule 1 to this Agreement for expenditures made (or, if the Bank shall so agree, to be made) in respect of the reasonable cost of goods and services required for the Project described in Schedule 2 to this Agreement and to be financed out of the proceeds of the Loan.

(b) The Borrower may, for the purposes of the Project, open and maintain in Dollars a special deposit account in a commercial bank acceptable to the Bank, on terms and conditions satisfactory to the Bank, including appropriate protection against set-off, seizure and attachment. Deposits into, and payments out of, the Special Account shall be made in accordance with the provisions of Schedule 4 to this Agreement.

Section 2.03. The Closing Date shall be December 31, 2003 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 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 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 January 15 and July 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. (a) The Borrower declares its commitment to the objectives of the Project as set forth in Schedule 2 to this Agreement, and, to this end, without any limitation or restriction upon any of its other obligations under the Loan Agreement, shall cause Shandong to perform in accordance with the provisions of the Project Agreement all the obligations of Shandong therein set forth, shall take or cause to be taken all action, including the provision of funds, facilities, services and other resources, necessary or appropriate to enable Shandong to perform such obligations, and shall not take or permit to be taken any action which would prevent or interfere with such performance.

(b) The Borrower shall make the proceeds of the Loan available to Shandong on the following principal terms:

- (i) the principal amount so made available to Shandong shall be the amount in Dollars (on the respective dates, of withdrawal from the Loan Account) of the value of the currency or currencies so withdrawn;
- (ii) Shandong shall repay such principal amount over a period of twenty (20) years, inclusive of a grace period of five (5) years;
- (iii) the Borrower 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 2.05 of this Agreement; and
- (iv) the Borrower 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.

Section 3.02. 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 the Project Agreement.

Section 3.03 The Bank and the Borrower hereby agree that 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 shall be carried out by Shandong pursuant to Section 2.03 of the Project Agreement.

ARTICLE IV

Financial Covenants

Section 4.01. (a) 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 or cause to be maintained in accordance with sound accounting practices, records and accounts reflecting such expenditures;
 - (ii) ensure that all records (contracts, orders, invoices, bills, receipts and other documents) evidencing such expenditures are retained until at least one year after the Bank has received the audit report for the fiscal year in which the last withdrawal from the Loan Account was made; and
 - (iii) enable the Bank's representatives to examine such records.
- (b) The Borrower shall:
- (i) have the records and accounts referred to in paragraph (a) (i) of this Section and those for the Special Account for each fiscal year audited, in accordance with appropriate auditing principles consistently applied, by independent auditors acceptable to the Bank;
 - (ii) furnish to the Bank as soon as available, but in any case not later than six months after the end of each such year the report of such audit by said auditors, of such scope and in such detail as the Bank shall have reasonably requested, including a separate opinion by said auditors as to whether the statements of expenditure submitted during such fiscal year, together with the procedures and internal controls involved in their preparation, can be relied upon to support the related withdrawals; 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.

ARTICLE V

Remedies of the Bank

Section 5.01. Pursuant to Section 6.02 (l) of the General Conditions, the following additional events are specified:

(a) Shandong shall have failed to perform any of its obligations under the Project Agreement.

(b) As a result of events which have occurred after the date of this Agreement, an extraordinary situation shall have arisen which shall make it improbable that Shandong will be able to perform its obligations under the Project Agreement.

(c) Any of the parties to the Financial Agency Agreement or any of the parties to any of the Subsidiary Loan Agreements shall have failed to perform any of its respective obligations thereunder.

(d) Any of the Basic Documents shall have been amended, suspended, abrogated, repealed or waived so as to affect materially and adversely the ability of the respective Utility Companies to perform any of its obligations under its respective Subsidiary Loan Agreement.

(e) The Borrower, Shandong or any other authority having jurisdiction, shall have taken any action for the dissolution or disestablishment of any of the Utility Companies or for the suspension of such entity's operations.

Section 5.02. Pursuant to Section 7.01 (h) of the General Conditions, the following additional events are specified:

(a) any event specified in paragraph (a) or (c) of Section 5.01 of this Agreement shall occur and shall continue for a period of sixty (60) days after notice thereof shall have been given by the Bank to the Borrower; and

(b) any event specified in paragraph (d) or (e) of Section 5.01 of this Agreement shall occur.

ARTICLE VI

Effective Date; Termination

Section 6.01. The following event is specified as an additional condition to the effectiveness of the Loan Agreement within the meaning of Section 12.01 (c) of the General Conditions, namely, that the Subsidiary Loan Agreements have been executed on behalf of the Project Municipalities and each of their respective Utility Companies.

Section 6.02. The following are specified as additional matters, within the meaning of Section 12.02 (c) of the General Conditions, to be included in the opinion or opinions to be furnished to the Bank:

(a) that the Project Agreement has been duly authorized or ratified by Shandong, and is legally binding upon Shandong in accordance with its terms; and

(b) that each of the Subsidiary Loan Agreements has been duly authorized or ratified by each of the parties thereto and is legally binding upon said parties in accordance with its terms.

Section 6.03. 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 Minister of Finance 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 Borrower:

Ministry of Finance
Sanlihe
Beijing 100820
People's Republic of China

Cable address:

FINANMIN
Beijing

Telex:

22486 MFPRC CN

For the Bank:

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

Cable address:

INTBAFRAD
Washington, D.C.

Telex:

248423 (MCI) or
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.

PEOPLE'S REPUBLIC OF CHINA

By /s/ Zhou Wenzhong

Authorized Representative

INTERNATIONAL BANK FOR
RECONSTRUCTION AND DEVELOPMENT

By /s/ Yukon Huang

Acting Regional Vice President
East Asia and Pacific

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) Works	30,000,000	40% of expenditures
(2) Goods (other than for Sub-projects)	50,000,000	100% of foreign expenditures, 100 % of local expenditures (ex-factory cost) and 75% of local expenditures for other items procured locally
(3) Goods under Sub-projects	5,000,000	100% of foreign expenditures, 100% of local expenditures (ex-factory cost) and 75% of local expenditures for other items procured locally

(4)	Consultants' services and training	5,000,000	100%
(5)	Unallocated	5,000,000	
		<u>95,000,000</u>	
	TOTAL	<u>=====</u>	

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 Borrower for goods or services supplied from the territory of any country other than that of the Borrower;

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

3. Notwithstanding the provisions of paragraph 1 above, no withdrawals shall be made in respect of :

(a) payments made for expenditures prior to the date of this Agreement, except that withdrawals in an aggregate amount not exceeding the equivalent of US\$1,500,000, may be made in respect of Categories (1), (2) and (4), set forth in the table in paragraph 1 of this Schedule on account of payment for expenditures before that date but after September 30, 1996;

(b) payments made for expenditures under Category 3, until the Bank shall have:

(i) approved the Operational Regulations; and

(ii) notified the Borrower of its acceptance of evidence that the Financial Agency Agreement has been executed on behalf of the parties thereto and is legally binding upon said parties in accordance with its terms; and

(c) payments made for expenditures under Category 1, until Shandong shall have entered into agreements, acceptable to the Bank and in accordance with Section II of Schedule 1 to the Project Agreement, with consultancy firms for the provision of: (i) institutional and financial technical assistance services under Parts E.1 (a) through (d) of the Project; and (ii) construction supervision services under parts E.1(a) through (e) of the Project.

4. The Bank may require withdrawals from the Loan Account to be made on the basis of statements of expenditure for expenditures:

- (a) for works under contracts costing less than \$2,500,000 equivalent each;
- (b) for goods under contracts costing less than \$500,000 equivalent each;
- (c) for consulting services under contracts awarded to consulting firms and costing less than \$100,000 each;
- (d) for consulting services under contracts awarded to individuals and costing less than \$50,000 each; and
- (e) for training regardless of the cost thereof;

all under such terms and conditions as the Bank shall specify by notice to the Borrower.

SCHEDULE 2

Description of the Project

The objectives of the Project are to assist Shandong to: (a) strengthen its policies, regulations and institutional arrangements for municipal water, wastewater, and district heating management and environmental pollution control; (b) improve water resource quality and management in the Xiaoqing river basin to allow for the optimal use of water resources for potable supply, industry and agriculture; (c) expand surface water supply to Jinan to prevent further depletion of groundwater aquifers; (d) facilitate sustainable management of investments in pollution control and municipally-provided urban environmental services.

The Project constitutes part of Shandong's long term environmental improvement program and consists of the following parts, subject to such modifications thereof as the Borrower and the Bank may agree upon from time to time to achieve such objectives:

Part A: Jinan

1. Water Supply Management

Improvement of the long-term reliability of Jinan's water supply system and protection of its groundwater resources, through the construction and equipping of:

(a) a settlement basin, comprising grit channels of about 700 meters wide and about 3.2 kilometers long, including earth embankments, access bridges, inlet/outlet gates, channels and pump stations of about 900,000 cubic meters per day capacity, and an outlet pipeline of about 2,000 millimeters diameter and 1.25 kilometers in length;

(b) a regulating reservoir, comprising an earth embanked storage of about 46 million cubic meters capacity, of about 7.2 meters average depth, with about 12 kilometers of embankments, ancillary equipment and facilities;

(c) transmission pipelines of about 1,200 to 2,000 millimeters diameter and about 16.2 kilometers in length, as well as a pumpstation of about 400,000 cubic meters per day capacity and ancillary facilities including distribution pipelines and related plant and equipment;

(d) a crossing of the Yellow River, and

(e) a highway diversion comprising upgrading of existing roads and construction of new roads of about 4.8 kilometers length.

2. Wastewater Management

Protection of the Xiaoqing river water quality and improved utilization of existing treatment facilities, through:

(a) construction and equipping of about 19 kilometers of trunk sewers and force mains with diameters of about 600 to 2,000 millimeters, siphons and ancillary facilities;

(b) construction and equipping of about 19 kilometers of secondary and link sewers with diameters of about 500 to 1,600 millimeters, siphons and ancillary facilities;

(c) construction and equipping of a pumpstation of about 100,000 cubic meters per day capacity for wastewater and about 81,000 cubic meters per day capacity for storm drainage, including screens, pumping equipment and ancillary facilities;

(d) construction and equipping of property connections in sizes to 300 millimeters diameter and about 11 kilometers in length and including local pumping wastewater management facilities; and

(e) provision of sewer cleaning and safety equipment as well as utility vehicles.

Part B: Weihai

Strengthening of Weihai's district heating system, through construction and equipping of:

1. a combined heat and power plant of about 24 megawatt electricity and about 120 megawatt heat capacity;

2. heat and steam networks, comprising about 13.7 kilometers of steam network of about 75 tons per hour capacity and hot water networks of about 14.2 kilometers of about 68 megawatt capacity; and

3. about 10 heat exchanger stations of varying capacity averaging about 6 megawatt.

Part C: Yantai

Strengthening of Yantai's district heating system, through construction and equipping of:

1. a boiler plant comprising boilers and associated equipment and facilities of about 112 megawatt capacity;

2. a heat network, comprising about 30 kilometers of heat network of about 500 megawatt capacity; and

3. about 42 heat exchanger stations of varying capacity averaging about 10 megawatt.

Part D: Industrial Pollution Control

The carrying out of sub-projects to upgrade in-plant technology processes of enterprises designed to reduce polluting discharges by said enterprises in order to comply with environmental regulations.

Part E: Institutional Development and Training

1. Strengthening the capacity of: (a) Jinan Water Company, (b) Jinan Drainage Company, (c) Weihai Company, (d) Yantai Company, (e) PPO, and (f) SEPB and SFB, in financial and institutional management, construction supervision, environmental protection, information management through the provision of equipment, consultants' services and training.

2. Carrying out an environmental data collection update with respect to water quality and management in the Xiaoqing river basin with a view to improving long-term environmental protection in the basin.

* * *

The Project is expected to be completed by December 31, 2002

SCHEDULE 3

Amortization Schedule

<u>Date Payment Due</u>	<u>Payment of Principal Expressed in Dollars*</u>
July 15, 2003	2,015,000
January 15, 2004	2,075,000
July 15, 2004	2,135,000
January 15, 2005	2,200,000
July 15, 2005	2,265,000
January 15, 2006	2,330,000
July 15, 2006	2,400,000
January 15, 2007	2,470,000
July 15, 2007	2,540,000
January 15, 2008	2,615,000
July 15, 2008	2,695,000
January 15, 2009	2,775,000
July 15, 2009	2,855,000
January 15, 2010	2,940,000
July 15, 2010	3,025,000
January 15, 2011	3,115,000
July 15, 2011	3,205,000
January 15, 2012	3,300,000
July 15, 2012	3,395,000
January 15, 2013	3,495,000
July 15, 2013	3,600,000
January 15, 2014	3,705,000
July 15, 2014	3,815,000
January 15, 2015	3,925,000
July 15, 2015	4,040,000
January 15, 2016	4,160,000
July 15, 2016	4,285,000
January 15, 2017	4,410,000
July 15, 2017	4,540,000
January 15, 2018	4,675,000

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

SCHEDULE 4

Special Account

1. For the purposes of this Schedule:

(a) the term “eligible Categories” means Categories 1 through 4 set forth in the table in paragraph 1 of Schedule 1 to this Agreement.

(b) the term “eligible expenditures” means expenditures in respect of the reasonable cost of goods and services required for the Project and to be financed out of the proceeds of the Loan allocated from time to time to the eligible Categories in accordance with the provisions of Schedule 1 to this Agreement; and

(c) the term “Authorized Allocation” means an amount equivalent to \$5,000,000 to be withdrawn from the Loan Account and deposited into the Special Accounts pursuant to paragraph 3 (a) of this Schedule, provided, however, that unless the Bank shall otherwise agree, the Authorized Allocation shall be limited to an amount equivalent to \$3,000,000 the aggregate amount of withdrawals from the Loan Account plus the total amount of all outstanding special commitments entered into by the Bank pursuant to Section 5.02 of the General Conditions shall be equal to or exceed the equivalent of \$25,000,000.

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

3. After the Bank has received evidence satisfactory to it that the Special Account has been duly opened, withdrawals of the Authorized Allocation and subsequent withdrawals to replenish the Special Account shall be made as follows:

(a) For withdrawals of the Authorized Allocation, the Borrower shall furnish to the Bank a request or requests for deposit into the Special Account of an amount or amounts which do not exceed the aggregate amount of the Authorized Allocation. On the basis of such request or requests, the Bank shall, on behalf of the Borrower, withdraw from the Loan Account and deposit into the Special Account such amount or amounts as the Borrower shall have requested.

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

(ii) Prior to or at the time of each such request, the Borrower shall furnish to the Bank the documents and other evidence required pursuant to paragraph 4 of this Schedule for the payment or payments in respect of which replenishment is requested. On the

basis of each such request, the Bank shall, on behalf of the Borrower, withdraw from the Loan Account and deposit into the Special Account such amount as the Borrower shall have requested and as shall have been shown by said documents and other evidence to have been paid out of the Special Account for eligible expenditures.

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

4. For each payment made by the Borrower out of the Special Account, the Borrower shall, at such time as the Bank shall reasonably request, furnish to the Bank such documents and other evidence showing that such payment was made exclusively for eligible expenditures.

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

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

(b) if the Borrower shall have failed to furnish to the Bank, within the period of time specified in Section 4.01 (b) (ii) of this Agreement, any of the audit reports required to be furnished to the Bank pursuant to said Section in respect of the audit of the records and accounts for the Special Accounts;

(c) if, at any time, the Bank shall have notified the Borrower of its intention to suspend in whole or in part the right of the Borrower to make withdrawals from the Loan Account pursuant to the provisions of Section 6.02 of the General Conditions; or

(d) once the total unwithdrawn amount of the Loan allocated to the eligible Categories, minus the total amount of all outstanding special commitments entered into by the Bank pursuant to Section 5.02 of the General Conditions with respect to the Project, shall equal the equivalent of twice the amount of the Authorized Allocation.

Thereafter, withdrawal from the Loan Account of the remaining unwithdrawn amount of the Loan allocated to the eligible Categories shall follow such procedures as the Bank shall specify by notice to the Borrower. Such further withdrawals shall be made only after and to the extent that the Bank shall have been satisfied that all such amounts remaining on deposit in the Special Account as of the date of such notice will be utilized in making payments for eligible expenditures.

6. (a) If the Bank shall have determined at any time that any payment out of the Special Account: (i) was made for an expenditure or in an amount not eligible pursuant to paragraph 2 of this Schedule; or (ii) was not justified by the evidence furnished to the Bank, the Borrower shall, promptly upon notice from the Bank: (A) provide such additional evidence as the Bank may request; or (B) deposit into the Special Account (or, if the Bank shall so request, refund to the Bank) an amount equal to the amount of such payment or the portion thereof not so eligible or justified. Unless the Bank shall otherwise agree, no further deposit by the Bank into the Special Account shall be made until the Borrower has provided such evidence or made such deposit or refund, as the case may be.

(b) If the Bank shall have determined at any time that any amount outstanding in the Special Account will not be required to cover further payments for eligible expenditures, the Borrower shall, promptly upon notice from the Bank, refund to the Bank such outstanding amount.

(c) The Borrower may, upon notice to the Bank, refund to the Bank all or any portion of the funds on deposit in the Special Account.

(d) Refunds to the Bank made pursuant to paragraphs 6 (a), (b) and (c) of this Schedule shall be credited to the Loan Account for subsequent withdrawal or for cancellation in accordance with the relevant provisions of this Agreement, including the General Conditions.