

CONFORMED COPY

LOAN NUMBER 2831 BR

Loan Agreement  
(Second Industrial Pollution Control Project)

between

FEDERATIVE REPUBLIC OF BRAZIL

and

INTERNATIONAL BANK FOR RECONSTRUCTION  
AND DEVELOPMENT

and

BANCO NACIONAL DE DESENVOLVIMENTO ECONOMICO E SOCIAL

Dated July 27, 1987

LOAN NUMBER 2831 BR

LOAN AGREEMENT

AGREEMENT, dated July 27, 1987, between FEDERATIVE REPUBLIC OF BRAZIL (the Borrower) and INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT (the Bank) and BANCO NACIONAL DO DESENVOLVIMENTO ECONOMICO E SOCIAL (BNDES).

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 whose Part B will be carried out by the Borrower through its Ministry of Urban Development and the Environment as hereinafter provided, by making the Loan as hereinafter provided;

(B) BNDES, a development bank wholly owned by, and created and operating under, the laws of the Borrower has been appointed by the Borrower as

its financial agent (agente financeiro) for purposes of the Project and, as such, BNDES has agreed to undertake such obligations towards the Bank as hereinafter provided including making available the proceeds of the Loan to the Project Entities (as the term is defined in Section 1.02 (u) of this Agreement) as hereinafter provided;

(C) Part A of the Project will be carried out in the State of Sao Paulo, a political subdivision of the Borrower (the State), with the Borrower's and the State's assistance and, as part of such assistance the Borrower will relend to the State, through BNDES, a portion of the proceeds of the Loan as provided in this Agreement, and in the terms and conditions provided in the Project Agreement referred to in (F) below;

(D) Part A of the Project will be carried out by Banco de Desenvolvimento do Estado de Sao Paulo S.A. - BADESP (BADESP), a development bank created and operating under the laws of the Borrower and the State and, in which the State owns, indirectly through Banco do Estado de Sao Paulo, S.A. (BANESPA), a majority interest and for that purpose, BNDES, as financial agent of the Borrower, will enter with BADESP, as financial agent (agente financeiro) of the State and administrator of PROCOP (as the term is defined in Section 1.02 (b) of this Loan Agreement), into an agreement on terms and conditions provided hereinafter and in the aforesaid Project Agreement under which, inter alia, part of the portion of the proceeds of the Loan to be re-lent to the State, as mentioned in C above, will be made available to BADESP for the carrying out of Part A.1 of the Project;

(E) Part A.2 of the Project will be carried out by CETESB Companhia de Tecnologia de Saneamento Ambiental (hereinafter called CETESB), a company in which the State owns a majority interest and has been created and is operating under the laws of the Borrower and the State, and for that purpose BADESP will make available to CETESB, as provided in the aforesaid Project Agreement, the remainder of the portion of the proceeds of the Loan re-lent to the State, through BADESP, under the agreement mentioned in (D) above;

(F) for purposes of the carrying out of Part A of the Project, the State, BADESP and CETESB have agreed to undertake, severally, certain obligations towards the Bank as are set forth in a Project Agreement of even date herewith between the Bank and the State and BADESP and CETESB (the Project 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;

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" of the Bank, dated January 1, 1985, with the modifications set forth in Schedule 4 to this Agreement (the General Conditions) constitute an integral part of this Agreement.

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) "Subsidiary Loan Agreement" means the agreement to be entered into between BNDES, on behalf and as financial agent of the Borrower, and the State and BADESP, pursuant to Section 3.01 (c) of this Agreement, as the same may be amended from time to time, and such term includes any schedule to the Subsidiary Loan Agreement;

(b) "FESB" means the State's Fundo Estadual de Saneamento Basico, a

fund established by the State's Lei No. 10107, dated May 8, 1968, as amended by Decreto-Lei No. 172, dated December 26, 1969, and by Lei No. 87, dated December 14, 1972, and as regulated by the State Decrees mentioned in paragraph (n) of this Section, by State Decree No. 14806, dated March 4, 1980, as amended by State Decree No. 21880, dated January 11, 1984, which set forth a program for purposes of financing the control of environmental pollution, by State Decrees No. 14807, dated March 4, 1980 and No. 21881, dated January 11, 1984, which established two sub-accounts, both within FESB and to be used as exclusive channels of funds specifically segregated for purposes of the aforementioned program, by Deliberacao No. 17/80 dated April 9, 1980, by State Decree No. 26972, dated April 29, 1987 under which the two sub-accounts in question were merged into one single sub-account (hereinafter called PROCOP), and by Deliberacao No. 23/87 of the State's Junta de Coordenacao Financeira, published in Diario Oficial do Estado de Sao Paulo on May 21, 1987, whereby BADESP has been appointed administrator of PROCOP effective as of April 30, 1987;

(c) "Sub-loan" means a loan to be financed partially or totally out of the proceeds of the Loan, made or proposed to be made by BADESP, as administrator of and out of funds credited to PROCOP, to an Investment Enterprise (as the term is defined in paragraph (e) below) for a Pollution Control Sub-project (as the term is defined in paragraph (g) below and, unless the context otherwise requires, the term refers indistinctively, to a Privileged Sub-loan or to a Non-Privileged Sub-loan, as these terms are defined below; "free-limit Sub-loan" means a Sub-loan, as so defined, which qualifies as a free-limit Sub-loan pursuant to the provisions of Section 2.02 (c) of this Agreement; "Privileged Sub-loan" means a Sub-loan, as so defined, that is made or intended to be made to an Old Investment Enterprise, as defined in paragraph (e) below, for a Direct Treatment Pollution Control Sub-Project, as defined in paragraph (g) below; and "Non-Privileged Sub-loan" means a Sub-loan, as so defined, other than a Privileged Sub-loan;

(d) "Grant" means a grant made or proposed to be made by BADESP, as Administrator of and out of funds credited to PROCOP, and to be financed out of the proceeds of the Loan, to CETESB of a Technical Assistance Sub-project (as the term is defined in paragraph (f) below), approved by or subject to the approval of, the Bank;

(e) "Investment Enterprise" means an entity eligible under the By-laws, including without limitation certain service enterprises, such as hospitals, hotels and waste disposal companies or joint ventures, and to which BADESP, as administrator of and out of funds credited to PROCOP, proposes to make or has made a Sub-loan; and the term "Old Investment Enterprise" means an Investment Enterprise, as so defined, except that its sources of industrial pollution in the State treated or to be treated under a Pollution Control Sub-project (as the term is defined in paragraph (g) below), were in operation in the State on or before December 31, 1986, except for the case of Pollution Control Sub-projects aiming at the control in GSPA (as the term is defined in paragraph (1) below) of particulate matter emission (including sulphur oxide particulates) where, in order to qualify as an Old Investment Enterprise, the sources of pollution to be treated under a Pollution Control Sub-project must have been in operation on or before April 14, 1980;

(f) "Technical Assistance Sub-project" means any project of the types described in Part A.2 of the Project, which is carried out or intended to be carried out by CETESB as part of its regular operations and utilizing the proceeds of a Grant;

(g) "Pollution Control Sub-project" means any specific pollution control project of the types described in Part A.1 of the Project which is carried out or intended to be carried out by an Investment Enterprise utilizing the proceeds of a Sub-loan; and "Direct Treatment Pollution Control Sub-project" means the physical, chemical or biological removal of pollution elements from plant emissions or effluents under a Pollution Control Sub-project;

(h) "Cruzado" means the currency unit of the Borrower;

(i) "Foreign expenditures" means expenditures in the currency of any

country other than the Borrower and for goods or services supplied from the territory of any country other than the Borrower; and "local expenditures" means expenditures in cruzados or for goods or services supplied from the territory of the Borrower;

(j) "State Pollution Control Legislation" means Law No. 898 of December 18, 1975, Law No. 997 of May 31, 1976 as amended by Law No. 1874 of December 8, 1978, Decree No. 8468 of September 8, 1976 as amended by Decree No. 15425 of July 23, 1980, Law No. 1172 of November 17, 1976, Decree No. 9714 of April 19, 1977, Decree No. 10229 of August 29, 1977 and Decree No. 10755 of November 22, 1977 as amended by Decree No. 24839 of March 6, 1986, all of the State;

(k) "Federal Pollution Control Legislation" means the Borrower's Decree Law No. 1413 dated August 14, 1975, as regulated by the Borrower's Decree No. 76389 dated October 3, 1975, and as further regulated by the Borrower's Decree No. 81107 dated December 2, 1977;

(l) "GSPA" means Regiao Metropolitana da Grande Sao Paulo, the greater Sao Paulo metropolitan area as defined in the Borrower's Lei Complementar No. 14 dated June 8, 1973;

(m) "CETESB's Legislation" means the State's Law No. 118 of June 29, 1973 and Decree No. 5993 of April 16, 1975 and the term includes all norms of the State Pollution Control Legislation and of the Estatutos of CETESB, as amended up to December 17, 1977, which empower CETESB to carry out its operations in accordance with CETESB's Legislation; provided, however, that without limitation or restriction to the rights of the Bank under paragraph (d) of Section 5.01 of this Agreement, the term will include additional amendments that may be made to CETESB's Estatutos from time to time after the date of this Agreement;

(n) "Steering Committee" means the Orientation Council of FESB composed of: the State's Secretaries of Works (Chairman), Environment, Metropolitan Affairs, Economy and Planning, Industry and Commerce, Science and Technology, and Finance, and representatives of BADESP, CETESB, SABESP and the Department of Water and Power (DAEE), as established by the State's Decree No. 907, dated December 29, 1972, as amended by Decrees No. 3351, dated February 13, 1974, No. 3436, dated March 20, 1974 and No. 14807, dated March 4, 1980, as amended by Decree No. 27020, dated May 22, 1987;

(o) "By-laws" means the By-laws of PROCOP approved by the State's Decree No. 27021, dated May 22, 1987 and the term includes any resolution of the Steering Committee consistent with the provisions of this Loan Agreement and of the Project Agreement that has been issued pursuant to said Decree No. 27021;

(p) "Reference Rate" means a nominal interest rate that, together with other charges applicable to the principal unpaid amount of a Sub-loan, is not lower than 9.5% per annum, and "Incentive Reference Rate" means a Reference Rate, as so defined, except that it is not lower than 6% per annum rather than not lower than 9.5% per annum, as this definition may be changed from time to time by notice from the Bank to BNDES with the prior approval of BADESP;

(q) "SABESP" means Companhia de Saneamento Basico do Estado de Sao Paulo - SABESP, a company created and operating under the laws of the Borrower and the State and on which the State owns a majority interest;

(r) "CESA" means the cruzado expenditures special account to be opened pursuant to Section 2.02 (b)(i) of this Agreement;

(s) "FESA" means the foreign exchange expenditures special account to be opened pursuant to Section 2.02 (b)(ii) of this Agreement;

(t) "Account Bank" means the Borrower's Central Bank (Central Bank) in respect of CESA and the commercial bank referred to in paragraph (b)(ii) of Section 2.02 of this Agreement, in respect of FESA;

(u) "Project Entity" means any of BADESP, CETESB and SEMA,

indistinctively;

(v) "SEPA" (State Environmental Protection Agency) means, in respect of any given State or Territory of the Borrower, the agency or administrative subdivision thereof that is the public entity in charge of pollution control activities within the jurisdiction of such State or Territory; and

(w) "SEMA" means Secretaria Especial do Meio Ambiente, an entity of direct administration established, by the Borrower's Decree No. 73,030 of October 30, 1973, as amended as of the date of this Agreement, within the Borrower's Ministry of Urban Development and the Environment; unless the context otherwise requires, the term "SEMA" shall be used in this Agreement to mean SEMA as a division of the referred Ministry through which the Borrower is carrying out Part B of the Project pursuant to paragraph (a) of Section 3.01 of this Agreement.

## 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 in various currencies equivalent to fifty million dollars (\$50,000,000).

Section 2.02. (a) The amount of the Loan may be withdrawn from the Loan Account by BNDES, on behalf of the Borrower, in respect of amounts paid (or, if the Bank shall so agree, for amounts to be paid):

(i) by BADESC, as administrator of PROCOP on account of withdrawals from PROCOP made by: (A) an Investment Enterprise under a Sub-loan, to meet the lower of: (I) 50% of the local expenditure and 100% of the foreign expenditures in respect of the reasonable cost of goods (other than vehicles, or non-imported computer equipment in the case of local expenditures), civil works, services and working capital required for the Pollution Control Sub-project in respect of which the withdrawal from the Loan Account is requested; or (II) 100% of the Sub-loan in respect of such Sub-project; or (B) CETESB, under a Grant to meet 100% of foreign expenditures in respect of the reasonable cost of goods (other than vehicles) and services required for the Technical Assistance Sub-project in respect of which the withdrawal from the Loan Account is requested; provided, however, that no withdrawal shall be made in respect of a Sub-loan or a Grant unless the Sub-loan or the Grant shall have been approved by the Bank, or the Sub-loan shall be a free-limit Sub-loan for which the Bank shall have authorized withdrawals from the Loan Account; and

(ii) SEMA to meet 100% of foreign expenditures and 50% of local expenditures in respect of the reasonable cost of goods (other than vehicles or non-imported computer equipment) or services, or both, required for Part B of the Project and that the Bank and SEMA have agreed to finance out of the proceeds of the Loan.

(b) The Borrower shall, for the purposes of the Project, open and thereafter maintain: (i) in the Central Bank an account in dollars on terms and conditions satisfactory to the Bank, (hereinafter called CESA), from which disbursements shall be made exclusively to meet expenditures in cruzados incurred in respect of the reasonable cost of goods and services required to carry out the Project and to be financed by the Bank pursuant to paragraph (a) above; and (ii) in a commercial bank acceptable to the Bank, an account in dollars, on terms and conditions satisfactory to the Bank, (hereinafter called FESA), from which disbursements shall be made exclusively to meet expenditures in currencies other than cruzados incurred in respect of the reasonable cost of goods and services required to carry out the Project and to be financed by the Bank pursuant to paragraph (a) above. Each of CESA and FESA shall have two Sub-accounts, one for recording entries corresponding to deposits or payments in

respect of Part A of the Project and the other for recording entries corresponding to deposits or payments in respect of Part B of the Project. These Sub-accounts will be kept by BNDES for the purposes of recording at all times the amounts on-lent by the Borrower under the Subsidiary Loan Agreement that would have been channeled through CESA or FESA, as the case may be. Deposits into, and payments out of, CESA and FESA shall be made in accordance with the provisions of Schedule 3 to this Agreement. The Borrower shall cause the Account Bank to furnish to the Bank each month certified statements of the CESA and FESA.

(c) A free-limit Sub-loan shall be a Sub-loan for a Pollution Control Sub-project to be financed out of proceeds of the Loan in an amount that shall not exceed the sum of \$2,000,000 equivalent, either by itself or when added to any other outstanding amounts financed or proposed to be financed for the Investment Enterprise in question or for a related Pollution Control Sub-project out of the proceeds of the Loan, the foregoing amount being subject to change from time to time as determined by the Bank.

(d) The aggregate amount of withdrawals to be made from the Loan Account shall not exceed: (i) in respect of Pollution Control Sub-projects, the equivalent of \$44,400,000; (ii) in respect of Technical Assistance Sub-projects, the equivalent of \$2,600,000; and (iii) in respect of expenditures under Part B of the Project, the equivalent of \$3,000,000.

(e) Except as the Bank and BNDES, and only in respect of Part A of the Project, BADESP also, shall otherwise agree, no withdrawals shall be made on account of:

(i) expenditures before the date of this Agreement, except that withdrawals may be made on account of payments made for expenditures prior to the date of this Agreement (A) under Pollution Control Sub-projects under Part A of the Project in respect of payments in an aggregate amount equivalent to \$4,000,000 made by BADESP before that day but after June 30, 1986, and (B) under Part B of the Project in respect of payments in an aggregate amount equivalent to \$200,000 made by SEMA before the date of this Agreement but after March 31, 1987; or

(ii) (A) expenditures by an Investment Enterprise in respect of a Sub-loan subject to the Bank's approval or expenditures by CETESB in respect of a Grant, if such expenditures shall have been made more than 180 days (in respect of Technical Assistance Sub-projects) or one year (in respect of Pollution Control Sub-projects) prior to the date on which the Bank shall have received: (1) in respect of such Sub-loan, the application and information required by Section 2.02 (a) of the Project Agreement; or (2) in respect of such Grant, the application and information required under Section 2.02 (c) of the Project Agreement; and (B) expenditures by an Investment Enterprise in respect of a free-limit Sub-loan, if such expenditures shall have been made more than one year prior to the date on which the Bank shall have received, in respect of such free-limit Sub-loan, the request and information required by Section 2.02 (b) of the Project Agreement; or

(iii) expenditures for Pollution Control or Technical Assistance Sub-projects unless: (A) the contractual arrangements referred to in Section 2.09 of the Project Agreement have been entered into, provided, however, that the contractual arrangements between CETESB and SABESP referred to in such Section shall condition only withdrawals in respect of Pollution Control Sub-projects related to the control of water pollutants in the GSPA; and (B) the Bank has received evidence satisfactory to the Bank that the Subsidiary Loan Agreement has been executed and delivered, including one or more opinions of counsel acceptable to the Bank on behalf of BNDES, as financial agent of the Borrower, and the State and BADESP, showing that the Subsidiary Loan Agreement has been duly authorized or ratified by, and executed

and delivered on behalf of BNDES, the State and BADESCP, respectively, and is legally binding upon BNDES and the Borrower, the State and BADESCP, respectively, in accordance with its terms; or (iv) expenditures under Part B of the Project unless the Bank has received evidence satisfactory to the Bank that the agreement referred to in Section 3.05 (b) of this Agreement has been executed and delivered, including an opinion of counsel acceptable to the Bank on behalf of SEMA, showing that such agreement has been duly authorized or ratified by, and executed and delivered on behalf of SEMA, and is legally binding upon SEMA and the other party to that Agreement in accordance with its terms; or

(v) expenditures under a contract for civil works estimated to cost the equivalent of \$5,000,000 or more.

Section 2.03. If, notwithstanding the provisions of Section 2.02 of this Agreement, in the opinion of the Bank and at any time: (i) the interest rate and other charges applicable to the principal unpaid amount of a Non-Privileged Sub-loan falls below the Reference Rate, or (ii) the interest rate and other charges applicable to the principal unpaid amount of a Privileged Sub-loan falls below the Incentive Reference Rate, or (iii) the adjustment of principal of a Sub-loan fails to be positive in relation to the prevailing inflation rate in Brazil, then the Bank shall have (A) the right, in the case of sub-paragraphs (i) or (iii) above, not to approve any Non-Privileged Sub-loan and not to authorize withdrawals from the Loan Account in respect of any Non-Privileged Sub-loan which qualifies as a free-limit Sub-loan, or (B) in the case of sub-paragraphs (ii) or (iii) above, the right not to approve any Privileged Sub-loan and not to authorize any withdrawal from the Loan Account in respect of any Privileged Sub-loan which qualifies a free-limit Sub-loan, until the Borrower, the State and the Bank have agreed on a new method of adjustment of the outstanding principal of Privileged or Non-Privileged Sub-loans, as the case may be, or on a new set of interest rates applicable to Privileged or Non-Privileged Sub-loans, as the case may be, or both, and if required, on the period within which such new method or rates, or both, shall be in effect, and shall have so notified BNDES and BADESCP.

Section 2.04. Except as the Borrower, the Bank, the State and BNDES shall otherwise agree:

(a) each application for approval of a Sub-loan (other than a free-limit Sub-loan), or a Grant, and each request for authorization to make withdrawals from the Loan Account in respect of a free-limit Sub-loan, shall be presented to the Bank by BADESCP, as administrator of PROCOP, in accordance with the provisions of paragraphs (a), (c) and (b), respectively, of Section 2.02 of the Project Agreement, and, when applicable of paragraph (d) of such Section;

(b) each such application or request shall be deemed presented or made by BNDES on behalf of the Borrower; and

(c) applications and requests made pursuant to the provisions of paragraphs (a) and (b) of this Section shall be presented to the Bank on or before September 30, 1990.

Section 2.05. The Closing Date shall be June 30, 1994 or such later date as the Bank shall establish. The Bank shall promptly notify the Borrower of such later date.

Section 2.06. 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 2.07. (a) The Borrower shall pay interest on the principal amount of the Loan withdrawn and outstanding from time to time at a rate per annum for each Interest Period equal to one-half of one percent per annum above the Cost of Qualified Borrowings for the last Semester ending prior to the commencement of such Interest Period.

(b) As soon as practicable after the end of each Semester, the Bank shall notify the Borrower of the Cost of Qualified Borrowings for such Semester.

(c) For purposes of this Section:

(i) "Interest Period" means the six-month period commencing on each date specified in Section 2.08 of this Agreement, including the Interest Period in which this Agreement is signed.

(ii) "Cost of Qualified Borrowings" means the cost of the outstanding borrowings of the Bank drawn down after June 30, 1982, expressed as a percentage per annum, as reasonably determined by the Bank.

(iii) "Semester" means the first six months or the second six months of a calendar year.

Section 2.08. Interest and other charges shall be payable semiannually on March 1 and September 1 in each year.

Section 2.09. The Borrower shall repay the principal amount of the Loan in accordance with the amortization schedule set forth in Schedule 1 to this Agreement.

Section 2.10. BNDES is designated as representative of the Borrower for the purposes of taking any action required or permitted to be taken under the provisions of Section 2.02 (a) of this Agreement and Article V of the General Conditions.

### 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, the Borrower shall carry out Part B of the Project, through its Ministry of Urban Development and the Environment acting through SEMA, with due diligence and efficiency and in conformity with appropriate administrative, financial and ecological practices, and shall provide, or cause to be provided, promptly as needed, funds and facilities, services and other resources required for Part B of the Project.

(b) Without any limitation or restriction upon any of its other obligations under the Loan Agreement, the Borrower shall cause the State, BADESP and CETESB to perform in accordance with the provisions of the Project Agreement all the respective obligations of the State, BADESP and CETESB therein set forth, shall take or cause to be taken all action necessary or appropriate to enable the State, BADESP and CETESB to perform such obligations, and shall not take or permit to be taken any action which would prevent or interfere with the aforesaid performances by the State, BADESP or CETESB.

(c) The Borrower shall, through BNDES, relend to the State the proceeds of the Loan withdrawn from time to time by BNDES on behalf of the Borrower pursuant to paragraph (a) (i) of Section 2.02 of this Agreement, under a subsidiary loan agreement to be entered into between BNDES, on behalf of the Borrower, and BADESP, on behalf of the State and as administrator of PROCOP, under terms and conditions satisfactory to the Bank which shall include financial obligations identical to those of the Borrower under the Loan plus a reasonable fee.

(d) BNDES shall exercise its rights under the Subsidiary Loan Agreement and comply with its obligations thereunder in such manner as to protect the interest of the Borrower, BNDES and the Bank and to accomplish the purposes of the Loan, and, except as the Bank shall otherwise agree, BNDES shall not assign, amend, abrogate or waive the Subsidiary Loan Agreement or any provision thereof.



(e) BNDES shall make available to SEMA the proceeds of the Loan withdrawn by BNDES on behalf of the Borrower pursuant to paragraph (a) (ii) of Section 2.02 of this Agreement.

Section 3.02. Except as the Bank shall otherwise agree, procurement of the goods, works (only in respect of Part A.1 of the Project) and consultants' services required for the Project and to be financed out of the proceeds of the Loan withdrawn by BNDES from the Loan Account pursuant to paragraph (a) of Section 2.02 of this Agreement, shall be governed by the provisions of the Schedule to the Project Agreement and, only in respect of Pollution Control Sub-projects, of paragraph (a) (ii) (1) of Section 2.07 of such 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 Part A of the Project shall be carried out by BADESP or CETESB, as the case may be, pursuant to Section 2.10 of the Project Agreement, while the same obligations in respect of Part B of the Project shall be carried out by the Borrower through SEMA.

Section 3.04. The Borrower shall cause Conselho Nacional do Meio Ambiente to make, by not later than December 31, 1988, a decision on any proposal made thereto by SEMA pursuant to paragraph (b)(iii) of Section 3.06 of this Agreement.

Section 3.05. Without limitation or restriction upon the provisions of paragraph (a) of Section 3.01:

(a) the Borrower shall, through SEMA, select from time to time the several SEPAS that will cooperate with SEMA in the carrying out of Part B of the Project, and except as the Borrower and the Bank have otherwise agreed, the Borrower shall cause SEMA to enter into an agreement with each SEPA so selected whenever the specific activities that the SEPA in question shall execute for purposes of Part B of the Project require that goods be procured by SEMA and be made available to such SEPA, either in the form of commodatum or as an assignment of SEMA's rights to the usage thereof, or fall under Part B (vi) of the Project; each such agreement shall stipulate the obligations of such SEPA, towards SEMA, in respect of the carrying out of Part B of the Project;

(b) the Borrower shall, through SEMA, enter into an agreement with an entity acceptable to the Bank on term and conditions satisfactory to the Bank under which SEMA shall be assisted in the procurement of equipment, consulting services, foreign training services or in other matters, all for Part B of the Project; and

(c) the Borrower shall cause SEMA to perform duly all its obligations under the agreements referred to in paragraphs (a) and (b) of this Section and, except as the Bank shall otherwise agree, shall cause SEMA not to take or to concur in any action which would have the effect of amending, abrogating, assigning or waiving any of such agreements or any provisions thereof.

Section 3.06. (a) The Borrower shall, through SEMA, carry out Parts B (ii), (iii), (iv) and (vi) of the Project under terms of reference satisfactory to the Bank.

(b) The Borrower shall, through SEMA: (i) not later than December 1, 1987, start the execution of Part B (ii), (iii) and (iv) of the Project with respect to at least 12 of the Borrower's States other than Sao Paulo; (ii) complete the execution of such Parts of the Project not later than December 1, 1989; (iii) complete the execution of Part B (vi) of the Project in a timely fashion so as to enable SEMA, after complying with sub-paragraph (iv) of this paragraph, to propose federal-level incentives for pollution control to the Conselho Nacional do Meio Ambiente by not later than September 30, 1988; and (iv) promptly upon the completion of each study for, and the preparation of each training program under the aforesaid parts of, the Project, furnish to the Bank copies of such studies and programs and give the Bank a reasonable opportunity

to comment on the results of such studies and content of such training programs.

#### ARTICLE IV

##### Financial and Other Covenants

Section 4.01. (a) BNDES shall, on behalf of the Borrower, maintain separate records and accounts adequate to reflect in accordance with sound accounting practices the operations, resources and expenditures of BNDES in respect of the Project:

(b) The Borrower shall, through SEMA, maintain separate records and accounts adequate to reflect in accordance with sound accounting practices, the operations, resources and expenditures of SEMA in respect of Part B of the Project;

(c) (i) BNDES shall, on behalf of the Borrower, maintain or cause to be maintained in accordance with sound accounting practices, separate records and accounts reflecting all expenditures in respect of which withdrawals are requested from the Loan Account on the basis of statement of 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; (iii) enable the Bank's representatives to examine such records; and (iv) furnish to each Project Entity, all such information,, including copy of each statement of expenditure submitted to the Bank in respect of withdrawals from the Loan account, as shall be convenient to enable such Project Entity to comply with the auditing requirements of such Project Entity under this Agreement or the Project Agreement, as the case may be;

(d) (i) BNDES, on behalf of the Borrower, shall have the accounts referred to in paragraphs (a) and (c) of this Section, the sub-accounts of FESA and CESA referred to in paragraph (b) of Section 2.02 of this Agreement and the FESA, and the Borrower shall have the accounts under paragraph (b) of this Section and the CESA, all for each fiscal year audited, in accordance with appropriate auditing principles consistently applied, by independent auditors acceptable to the Bank; and (ii) BNDES, and the Borrower through SEMA, as the case may be, shall furnish to the Bank as soon as available, but in any case not later than four 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 in respect of the records and accounts referred to in paragraphs (a) and (c) (i) (BNDES), and (b) (SEMA) of this Section as to whether the proceeds of the Loan withdrawn in respect of such expenditures were used for the purposes for which they were provided; and

(e) for all expenditures with respect to which withdrawals from the Loan Account for purposes of Part B of the Project were made on the basis of statements of expenditure, the Borrower through SEMA shall:

(i) maintain or cause to be maintained, in accordance with paragraph (b) of this Section, records and accounts reflecting such expenditures;

(ii) retain, until at least one year after the Bank has received the audit report for the fiscal year in which the last withdrawal from the Loan Account was made, all records (contracts, orders, invoices, bills, receipts and other documents) evidencing such expenditures;

(iii) enable the Bank's representatives to examine such records; and

(iv) ensure that such records and accounts are included in the annual audit referred to in paragraph (d) of this Section and that the report of such audit contains a separate opinion

by said auditors as to whether the statements of expenditure submitted during such fiscal year, together with the procedures and internal controls involved in their preparation, can be relied upon to support the related withdrawals.

Section 4.02. If the Borrower shall have, pursuant to the Federal Pollution Control Legislation and notwithstanding a petition of the State to the contrary, determined, rejected or cancelled the suspension of operations of a plant in the State of Sao Paulo, the Borrower shall, through SEMA, promptly inform the Bank and BNDES of its decision on the case and shall furnish the Bank all information on such case as the Bank shall reasonably request.

#### ARTICLE V

##### Remedies of the Bank

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

(a) BNDES shall have failed to perform any of its obligations under this Agreement;

(b) the State, BADESC or CETESB shall have failed to perform any of their respective obligations under the Project Agreement;

(c) any authority having jurisdiction shall have taken any action for the dissolution or disestablishment of BNDES, SEMA, BADESC or CETESB; provided, however, that this paragraph shall not apply if any institution so dissolved or disestablished shall have been succeeded by an institution, acceptable to the Bank, which shall have assumed all the obligations and acquired all the rights provided for in this Agreement or in the Project Agreement, or both, as the case may be, in respect of the institution so dissolved or disestablished;

(d) a change in any Lei or Decree of the State or Deliberacao referred to or mentioned in paragraph (b) or paragraph (n) of Section 1.02 of this Agreement, or in the By-laws, or in the State Pollution Control Legislation, or in CETESB's Legislation, or in the Federal Pollution Control Legislation, shall have been made, or the lack of enforcement thereof, or of further pollution control legislation enacted by the Borrower or the State, or of regulations thereof shall have occurred, which shall have affected materially and adversely the carrying out of the Project;

(e) an extraordinary situation shall have arisen which shall make it improbable that the State, BNDES, SEMA (acting as an agent of the Borrower), BADESC or CETESB will be able to perform its obligations under this Agreement or under the Project Agreement, as the case may be;

(f) SEMA shall have changed without the consent of the Bank the contractual arrangements referred to in Section 3.05 (b) of this Agreement, or shall have failed to perform any of its respective obligations thereunder; provided, however, that the right of the Bank to suspend the right of the Borrower to make withdrawals from the Loan Account shall be limited to: (A) withdrawals to be made pursuant to paragraph (a) (i) of Section 2.02 of this Agreement, when the event in question shall have been specified in paragraphs (b) or (c) or (e) of this Section and relates exclusively to the State, BADESC or CETESB; or (B) withdrawals to be made pursuant to paragraph (a) (ii) of Section 2.02 of this Agreement, when the event in question shall have been specified in paragraphs (c) or (e) of (f) of this Section and relates exclusively to SEMA.

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 paragraph (b) or paragraph (f) of Section 5.01 of this Agreement shall occur and shall continue for a period of sixty days after notice thereof shall have been given by the Bank to the Borrower; and

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

#### ARTICLE VI

##### Effective Date; Termination

Section 6.01. 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) that this Agreement has been duly registered by Banco Central do Brasil; and

(b) that all necessary acts, consents and approvals to be performed or given by the Borrower, its agencies or political subdivisions, including BNDES and the State, respectively, by any agency thereof, including BADESC and CETESB, or otherwise to be Performed or given in order to authorize the carrying out of the Project and to enable the Borrower or BNDES, and the State, BADESC or CETESB to perform their obligations pursuant to this Agreement and to the Project Agreement, respectively, together with all necessary powers and rights in connection therewith, have been performed or given.

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 the State, BADESC and CETESB and is legally binding upon the State, BADESC and CETESB in accordance with its terms; and

(b) that all necessary acts, consents and approvals to be performed or given by the Borrower or the State, their political subdivisions or agencies, including BNDES, BADESC and CETESB, or by any agency thereof or otherwise to be performed or given in order to authorize the carrying out of the Project and to enable the Borrower, BNDES, the State, BADESC and CETESB to perform their respective obligations pursuant to this Agreement and to the Project Agreement, together with all necessary powers and rights in connection therewith, have been performed or given.

Section 6.03. The date November 26, 1987 is hereby specified for the purposes of Section 12.04 of the General Conditions.

#### ARTICLE VII

##### Representatives of the Borrower and BNDES; Addresses

Section 7.01. Except as provided in Section 2.02 (a) of this Agreement, 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:

Ministerio da Fazenda  
Edificio Ministerio da Fazenda  
Esplanada dos Ministerios  
70048 - Brasilia, DF  
Brasil

Cable address:

Telex:

MINIFAZ  
Brasilia, Brasil

611506

with copy to:

Ministry of Urban Development  
and the Environment  
Avenida W/3 Norte Quadra 505  
Bloco B-3 Andar  
70000 - Brasilia, DF  
Brazil

Cable address:

MINIFAZ  
Brasilia, Brasil

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:

440098 (ITT)  
248423 (RCA) or  
64145 (WUI)

For BNDES:

Banco Nacional de Desenvolvimento  
Economico e Social  
Avenida Republica do Chile, 100  
20139 - Rio de Janeiro, RJ  
Brasil

Cable address:

BADEC  
Rio de Janeiro, Brazil

Telex

0213389-BNDES BR

Section 7.03. (a) Any action required or permitted to be taken, and any document required or permitted to be executed, under this Agreement on behalf of BNDES may be taken or executed by its President or such other person or persons as provided by BNDES's By-laws, or both. BNDES shall designate in writing, and BNDES shall furnish to the Bank sufficient evidence of the authority and the authenticated specimen signature of each such person.

(b) Any action taken by BNDES in accordance with paragraph (a) above pursuant to any of the provisions of this Agreement shall be deemed, for purposes of this Agreement, taken on behalf of the Borrower.

IN WITNESS WHEREOF, the parties hereto, acting through their duly authorized representative, 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.

FEDERATIVE REPUBLIC OF BRAZIL

By /s/ Luiz Carlos Bresser Pereira  
Authorized Representative

INTERNATIONAL BANK FOR  
RECONSTRUCTION AND DEVELOPMENT

By /s/ S. Shahid Husain

Regional Vice President  
Latin America and the Caribbean

BANCO NACIONAL DO DESENVOLVIMENTO  
ECONOMICO E SOCIAL

By /s/ Jose Araujo Penna

Authorized Representative

SCHEDULE 1

Amortization Schedule

Date Payment Due	Payment of Principal (Expressed in dollars)*
on each March 1 and September 1 beginning March 1, 1991 through March 1, 2002	2,085,000
On September 1, 2002	2,045,000

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\* The figures in this column represent dollar equivalents determined as of the respective dates of withdrawal. See General Conditions, Sections 3.04 and 4.03.

Premiums on Prepayment

The following premiums are specified for the purposes of Section 3.04 (b) of the General Conditions:

Time of Prepayment	Premium
	The interest rate (expressed as a percentage per annum) applicable to the balance outstanding on the Loan on the day of prepayment multiplied by:
Not more than three years before maturity	0.20
More than three years but not more than six years before maturity	0.40
More than six years but not more than eleven years before maturity	0.73
More than eleven years but not more than thirteen years before maturity	0.87
More than thirteen years before maturity	1.00

SCHEDULE 2

Description of the Project

The objectives of the Project are to improve public health by reducing industrial air, water and solid waste pollution within the State and to strengthen SEMA and selected SEPAS, including CETESB, by developing these agencies operational and technical capabilities to design and implement integrated long-term industrial pollution control strategies and programs within their respective jurisdiction.

The Project 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: Sao Paulo Component

1. A program for the identification and preparation of Pollution Control Sub-projects, and for the carrying out of Pollution Control Sub-projects for which Sub-loans have been approved, or in respect of which disbursements from the Loan Account have been authorized. The Sub-projects will be carried out through Investment Enterprises operating within the State which: (i) in order to comply with the State Pollution Control Legislation and, when applicable, with any specific pollution control strategy agreed from time to time between the Bank and CETESB for purposes of the Project, undertake industrial pollution control activities such as: (a) the treatment or pre-treatment of their effluents and emission discharges, or (b) the substantial change of their technological or productive processes or (c) the disposal of their industrial solid or liquid wastes, or (d) other environmental industrial pollution control activities; or (ii) are required by CETESB to relocate, or relocate voluntarily contributing by such relocation, if so determined by CETESB, to pollution control, or (iii) provide industrial solid waste disposal services' (other than ordinary garbage collection services) to third parties.

2. A program for the identification, preparation and carrying out of

Technical Assistance Sub-projects approved by the Bank and by CETESB such as: (i) acquisition and utilization of specific and specialized, training, monitoring and laboratory analysis equipment; (ii) applied research and studies in fields of biological and toxic treatment, hazardous risk assessment and cost benefit analysis of pollution control solutions; and (iii) training of staff from industrial enterprises and CETESB in various pollution control subjects.

Part B: Federal Component

This component will be carried out in respect of several of the Borrower's States, other than Sao Paulo, as selected by SEMA from time to time, and of SEMA, and in cooperation with the corresponding SEPA. It will include: (i) the acquisition by SEMA, and utilization by the SEPA in question, of equipment for laboratories and monitoring programs; (ii) the execution of diagnostic studies to determine the nature and extent of industrial pollution problems in the State in question, with recommendations for control strategies and to assess the operational capabilities of each State's SEPA; (iii) the assessment of training resources available in the State in question and in the corresponding SEPA; (iv) design of technical assistance programs to help each State's SEPA achieve its operational objectives; (v) execution of technical assistance programs to develop the capabilities in pollution control of SEMA and selected SEPAs other than CETESB; and (vi) development by SEMA of appropriate incentives for investments in pollution control solutions.

SCHEDULE 3

CESA and FESA Accounts

1. For the purposes of this Schedule:

(a) the term "Categories" means a category of items to be financed out of the proceeds of the Loan pursuant to paragraph (d) of Section 2.02 of 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 Section 2.02 of this Agreement; and

(c) the term "Authorized Allocation" means an amount equivalent to not more than \$5,000,000 and to not more than \$300,000 to be withdrawn from the Loan Account and deposited in the CESA and FESA, respectively, pursuant to paragraph 3 (a) of this Schedule.

2. Except as the Bank shall otherwise agree, payments out of CESA or FESA, as the case may be, shall be made exclusively for eligible expenditures in accordance with the provisions of this Schedule. The Account Bank shall authorize withdrawals from the CESA or FESA, as the case may be, on the basis of the evidence that the Bank shall have reasonably determined. For each such withdrawal so authorized, the Account Bank shall debit or cause to be debited CESA or FESA, as the case may be, with the dollar equivalent of the amount of the eligible expenditures in question in cruzados, in the case of CESA, or with the actual dollar amount or the dollar equivalent of the eligible expenditures in currencies other than dollars or cruzados, in the case of FESA.

3. After the Bank has received evidence satisfactory to it that CESA or FESA, as the case may be, and their corresponding Sub-accounts for Parts A and B of the Project have been duly opened, withdrawals of the corresponding Authorized Allocation and subsequent withdrawals to replenish CESA or FESA, as the case may be, may be made as follows:

(a) on the basis of a request or requests by the Borrower for a deposit or deposits which add up to the aggregate amount of the Authorized Allocation, the Bank shall, on behalf of the Borrower, withdraw from the Loan Account and deposit in CESA or FESA, as the case may be, for the crediting of the corresponding Sub-account for Part A or Part B of the Project, such amount or



amounts as the Borrower shall have requested.

(b) The Borrower shall furnish to the Bank requests for replenishment of CESA and FESA, as the case may be, at such intervals as the Bank shall specify. On the basis of such requests, the Bank shall withdraw from the Loan Account and deposit into CESA or FESA, for the crediting of the corresponding Sub-account for Part A or Part B of the Project, such amounts as shall be required to replenish CESA or FESA, as the case may be, with amounts not exceeding the amount of payments made out of CESA or FESA, as the case may be, for eligible expenditures. All such deposits shall be withdrawn by the Bank from the Loan Account in the respective equivalent amounts as shall have been justified by the evidence supporting the request for such deposit furnished pursuant to paragraph 4 of this Schedule.

4. For each payment made by the Borrower out of CESA or FESA, for which the Borrower requests replenishment pursuant to paragraph 3 (b) of this Schedule, the Borrower shall furnish to the Bank, prior to or at the time of such request, such documents and other evidence as the Bank shall reasonably request, showing that such payment was made for eligible expenditures.

5. (a) Notwithstanding the provisions of paragraph 3 of this Schedule, the Bank may deny any request for further deposits into CESA or FESA when either of the following situations arises:

(i) 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; or

(ii) the total unwithdrawn amount of the Loan allocated to the eligible Categories, in respect of Part A or Part B of the Project, as the case may be, minus the amount of any outstanding special commitment entered into by the Bank pursuant to Section 5.02 of the General Conditions with respect to the corresponding Part of the Project, shall be equal to the equivalent of twice the amount of the Authorized Allocation credited to the corresponding Sub-account of CESA or FESA, as the case may be.

(b) 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 CESA or FESA, as the case may be, 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 CESA or FESA (i) was made for any expenditure or in any amount not eligible pursuant to paragraph 2 of this Schedule, or (ii) was not justified by the evidence furnished pursuant to paragraph 4 of this Schedule, the Borrower shall, promptly upon notice from the Bank, deposit into the corresponding Subaccount of CESA or FESA, as the case may be, (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. No further deposit by the Bank into CESA or FESA shall be made until the Borrower shall have made such deposit or refund.

(b) If the Bank shall have determined at any time that any amount outstanding in CESA or FESA 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 for crediting to the Loan Account and immediate cancellation.

#### SCHEDULE 4

#### Modifications of the General Conditions

For the purposes of the Loan Agreement, the provisions of the General Conditions are modified as follows:

(1) Paragraph 11 of Section 2.01 is deleted and replaced by the following new paragraph:

"11. The term 'Project' means the project or program for which the Loan is granted, as described in the Loan Agreement and as the description thereof may be amended from time to time by agreement between the Borrower, the Bank and, in respect of Part A thereof, the State of Sao Paulo."

(2) The last sentence of Section 3.02 is deleted.

(3) Section 6.03 is deleted and replaced by the following new Section:

"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) by the date specified in paragraph (c) of Section 2.04 of the Loan Agreement no applications or requests permitted under, or referred to in, paragraphs (a) and (b) of such Section and paragraphs (a) through (c) of Section 2.02 of the Project Agreement (as the term is defined in the Loan Agreement) shall have been received by the Bank in respect of any portion of the Loan, or having been so received, shall have been denied, or (c) after the Closing Date an amount of the Loan shall remain unwithdrawn from the Loan Account, the Bank may by notice the Borrower terminate the right of the Borrower to submit such applications or requests or to make withdrawals from the Loan Account, as the case may be, with respect to such amount or portion of the Loan. Upon the giving of such notice such amount or portion of the Loan shall be cancelled."

(4) Each reference to the Borrower in paragraphs (a) and (b) of Section 9.01 shall be read as a reference to the Borrower, BNDES and SEMA.

