

CONFORMED COPY

CREDIT NUMBER 2868 KG

Project Agreement

(Power and District Heating Rehabilitation Project)

between

INTERNATIONAL DEVELOPMENT ASSOCIATION

and

KYRGYZ NATIONAL ENERGY HOLDING COMPANY

Dated July 3, 1996

CREDIT NUMBER 2868 KG

PROJECT AGREEMENT

AGREEMENT, dated July 3, 1996, between INTERNATIONAL DEVELOPMENT ASSOCIATION (the Association) and KYRGYZ NATIONAL ENERGY HOLDING COMPANY (KNEHC).

WHEREAS (A) by the Development Credit Agreement of even date herewith between Kyrgyz Republic (the Borrower) and the Association, the Association has agreed to make available to the Borrower an amount in various currencies equivalent to thirteen million six hundred thousand Special Drawing Rights (SDR13,600,000), on the terms and conditions set forth in the Development Credit Agreement, but only on condition that KNEHC agree to undertake such obligations toward the Association as are set forth in this Agreement; and

(B) by a subsidiary loan agreement to be entered into between the Borrower and KNEHC, part of the proceeds of the credit provided for under the Development Credit Agreement will be made available to KNEHC on the terms and conditions set forth in said Subsidiary Loan Agreement; and

WHEREAS KNEHC, in consideration of the Association's entering into the Development Credit Agreement with the Borrower, has agreed to undertake the obligations set forth in this Agreement;

NOW THEREFORE the parties hereto hereby agree as follows:

ARTICLE I

Definitions

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

ARTICLE II

Execution of the Project

Section 2.01. KNEHC declares its commitment to the objectives of the Project as set forth in Schedule 2 to the Development Credit Agreement, and, to this end, shall carry out Parts A and D of the Project with due diligence and efficiency and in conformity with appropriate administrative, financial, engineering, environmental and public utility practices, and shall provide, or cause to be provided, promptly as needed, the funds, facilities, services and other resources required for Parts A and D of the Project.

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

Section 2.03. (a) KNEHC shall carry out the obligations set forth in: (i) Sections 9.03 and 9.04 of the General Conditions (relating to insurance and use of goods and services, respectively) in respect of the Project Agreement and Parts A and D of the Project; and (ii) Sections 9.05, 9.06, 9.07 and 9.08 of the General Conditions (relating to plans and schedules, records and reports, maintenance and land acquisition, respectively) in respect of the Project Agreement and Parts A through D of the Project;

(b) For the purpose of Section 9.07 of the General Conditions, and without limitation thereto, and taking into account the provisions of Section 3.03 of the Development Credit Agreement, KNEHC shall:

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

Section 2.04. KNEHC shall duly perform all its obligations under the Subsidiary Loan Agreement. Except as the Association shall otherwise agree, KNEHC shall not take or concur in any action which would have the effect of amending, abrogating, assigning or waiving the Subsidiary Loan Agreement or any provision thereof.

Section 2.05. (a) KNEHC shall, at the request of the Association, exchange views with the Association with regard to the progress of the Project, the performance of its obligations under this Agreement and under the Subsidiary Loan Agreement, and other matters relating to the purposes of the Credit.

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

Section 2.06. KNEHC shall maintain the PIU with a sufficient number of qualified staff and adequate facilities, as satisfactory to the Association.

Section 2.07. By December 31, 1996, KNEHC shall appoint consultants, whose qualifications and terms of reference shall be satisfactory to the Association, to assist in: (i) carrying out a billing and collection study; (ii) reviewing with the Association the findings and recommendations of such study, and schedule of implementation attached thereto; and (iii) carrying out the recommendations, agreed with the Association in accordance with said schedule of implementation.

Section 2.08. KNEHC shall appoint consultants, whose qualifications and terms of reference shall be satisfactory to the Association, to assist KNEHC and the Borrower in carrying out the implementation plan for the organization of the power and heat sector referred to in Section 4.06 (iii) of the Development Credit Agreement.

ARTICLE III

Management and Operations of KNEHC

Section 3.01. KNEHC shall carry on its operations and conduct its affairs in accordance with sound administrative, financial and public utility practices under the supervision of qualified and experienced management assisted by competent staff in adequate numbers.

Section 3.02. KNEHC shall at all times operate and maintain its plant, machinery, equipment and other property, and from time to time, promptly as needed, make all necessary repairs and renewals thereof, all in accordance with sound engineering, financial and public utility practices.

Section 3.03. KNEHC shall take out and maintain with responsible insurers, or make other provision satisfactory to the Association for, insurance against such risks and in such amounts as shall be consistent with appropriate practice.

ARTICLE IV

Financial and Other Covenants

Section 4.01. (a) KNEHC shall maintain records and accounts adequate to reflect in accordance with sound accounting practices its operations and financial condition.

(b) KNEHC shall:

- (i) have its records, accounts and financial statements (balance sheets, statements of income and expenses and related statements) for each fiscal year audited, in accordance with appropriate auditing principles consistently applied, by independent auditors acceptable to the Association;
- (ii) furnish to the Association as soon as available, but in any case not later than six (6) months after the end of each such year, (A) certified copies of its financial statements for such year as so audited and (B) the report of such audit by said auditors, of such scope and in such detail as the Association shall have reasonably requested; and
- (iii) furnish to the Association such other information concerning said records, accounts and financial statements as well as the audit thereof, as the Association shall from time to time reasonably request.

Section 4.02. KNEHC shall:

(a) review with the Association, by October 31 of each year starting in 1996, KNEHC's proposed investment program for the following five years; and

(b) consider and take into account the Association's views in finalizing said program.

Section 4.03. KNEHC shall: (i) by January 1, 1997, enter into agreements, or otherwise make appropriate arrangements, with consumers providing for the exclusive ownership by KNEHC of new power and heat meters and for the obligations of consumers to pay a monthly fee therefor; and (ii) by January 1, 1998, ensure that all power consumers are metered.

Section 4.04. KNEHC shall:

(a) maintain policies and procedures adequate to enable it to monitor and evaluate on an ongoing basis, in accordance with indicators satisfactory to the Association, the carrying out of the Project, and the achievement of the objectives thereof;

(b) prepare, under terms of reference satisfactory to the Association, and furnish to the Association, on or about June 30, 1998, a report integrating the results of the monitoring and evaluation activities performed pursuant to paragraph (a) of this Section, on the progress achieved in the carrying out of the Project during the period preceding the date of said report and setting out the measures recommended to ensure the efficient carrying out of the Project and the achievement of the objectives thereof during the period following such date; and

(c) review with the Association by September 30, 1998, or such later date as the Association shall request, the report referred to in paragraph (b) of this Section, and thereafter, take all measures required to ensure the efficient completion of the Project and the achievement of the objectives thereof, based on the conclusions and recommendations of the said report and the Association views on the matter.

Section 4.05. KNEHC shall carry out a program of actions in accordance with the environmental management plan agreed with the Association with due diligence and efficiency, and submit to the Association the reports required under such environmental management plan.

Section 4.06. For each fiscal year after that ending on December 31, 1995, KNEHC shall prepare separate financial statements for its power and heat activities, in addition to its consolidated financial statements.

Section 4.07. By December 31, 1996, on the basis of a methodology satisfactory to the Association, and in conjunction with the study on power and heat tariffs referred to in Section 4.04 of the Development Credit Agreement, KNEHC shall conduct a re-valuation of its assets and have the same reflected in its balance sheets dated December 31, 1995.

Section 4.08. KNEHC shall take all actions required on its part to ensure that its accounts receivable, both for power and heat, shall not exceed the equivalent of: (i) 90 days of its average annual billing by December 31, 1996; and (ii) 60 days of its average annual billing by December 31, 1997 and thereafter.

Section 4.09. By October 31 of each year, KNEHC shall submit to the Association, for its review, an operating and capital budget for the following year, with the indication of its financing sources.

Section 4.10. (a) Except as the Association shall otherwise agree, KNEHC shall not incur any debt unless a reasonable forecast of the revenues and expenditures of KNEHC shows that the estimated net revenues of KNEHC for each fiscal year during the term of the debt to be incurred shall be at least 1.5 times the estimated debt service requirements of KNEHC in such year on all debt of KNEHC including the debt to be incurred.

(b) For the purposes of this Section:

- (i) The term "debt" means any indebtedness of KNEHC maturing by its terms more than one year after the date on which it is originally incurred.
- (ii) Debt shall be deemed to be incurred: (A) under a loan contract or agreement or other instrument providing for such debt or for the modification of its terms of payment on the date of such contract, agreement or instrument; and (B) under a guarantee agreement, on the date the agreement providing for such guarantee has been entered into.
- (iii) The term "net revenues" means the difference between: (A) the sum of revenues from all sources related to operations and net non-operating income; and (B) the sum of all expenses related to operations including administration, adequate maintenance, taxes and payments in lieu of taxes, but excluding provision for depreciation, other non-cash operating charges and interest and other charges on debt.
- (iv) The term "net non-operating income" means the difference between: (A) revenues from all sources other than those related to operations; and (B) expenses, including taxes and payments in lieu of taxes, incurred in the generation of revenues in (A) above.
- (v) The term "debt service requirements" means the aggregate amount of repayments (including sinking fund payments, if any) of, and interest and other charges on, debt.
- (vi) The term "reasonable forecast" means a forecast prepared by KNEHC not earlier than twelve months prior to the incidence of the debt in question, which both the Association and KNEHC accept as reasonable and as to which the Association has notified KNEHC of its acceptability, provided that no event has occurred since such notification which has, or may reasonably be expected in the future to have, a material adverse effect on the financial condition or future operating results of KNEHC.
- (vii) Whenever for the purposes of this Section it shall be necessary to value, in terms of the currency of the Borrower, debt payable in another currency, such valuation shall be made on the basis of the prevailing lawful rate of exchange at which such other currency is, at the time of such valuation, obtainable for the purposes of servicing such debt, or, in the absence of such rate, on the basis of a rate of exchange acceptable to the Association.

Section 4.11. (a) KNEHC shall generate revenues that will cover its total operating expenses, including depreciation, in 1997.

(b) For the purposes of this Section:

- (i) the term "total operating expenses" means all expenses related to operations, including administration, adequate maintenance, taxes and payments in lieu of taxes, and provision for depreciation on a reasonable basis, but excluding interest and other charges on debt;
- (ii) "debt" means any debt, including debt assumed or guaranteed by KNEHC, maturing more than one year after the date on which it is originally incurred;

and

- (iii) debt shall be deemed incurred: (A) under a loan contract or agreement or other instrument providing for such debt or for the modification of its terms of payment on the date of such contract, agreement or instrument; and (B) under a guarantee agreement, on the date the agreement providing for such guarantee has been entered into.

Section 4.12. (a) Except as the Association may otherwise agree, and subject to paragraph (c) of this Section, KNEHC shall produce, for each of its fiscal years after that ending on December 31, 1997, funds from internal sources equivalent to not less than thirty percent (30%) of KNEHC's annual capital expenditures incurred for that year.

(b) For the purposes of paragraph (a) of this Section:

- (i) the term "funds from internal sources" means the difference between: (x) the sum of revenues from all sources related to operations, net non-operating income and any reduction in working capital other than cash; and (y) the sum of all expenses related to operations, including administration, adequate maintenance, and taxes and payments in lieu of taxes (excluding provision for depreciation and other non-cash operating charges), debt-service requirements, all cash dividends and other cash distributions of surplus, increase in working capital other than cash, and other cash outflows other than capital expenditures;
- (ii) the term "net non-operating income" means the difference between revenues from all sources other than those related to operation, and expenses, including taxes and payments in lieu of taxes, incurred in the generation of revenues;
- (iii) the term "working capital other than cash" means the difference between current assets excluding cash and current liabilities at the end of each fiscal year;
- (iv) the term "current assets excluding cash" means all assets other than cash which could in the ordinary course of business be converted into cash within twelve months, including accounts receivable, marketable securities, inventories and prepaid expenses properly chargeable to operating expenses within the next fiscal year;
- (v) the term "current liabilities" means all liabilities which will become due and payable or could under circumstances then existing be called for payment within twelve months, including accounts payable, customer advances, debt-service requirements, taxes and payments in lieu of taxes, and dividends;
- (vi) the term "debt-service requirements" means the aggregate amount of repayments (including sinking-fund payments, if any), interest and other charges on debt; and
- (vii) the term "capital expenditures" means all expenditures incurred on account of fixed assets, including interest charged to construction, related to operations.

(c) For the purpose of monitoring compliance with the provisions of Section 4.12 (a), the requirement to produce funds from internal sources equivalent to not less than thirty percent (30%) of annual capital expenditures will be deemed to be satisfied in respect

of a particular fiscal year if the average ratio of funds from internal sources to annual capital expenditures for that fiscal year, the previous fiscal year and the next fiscal year equals or exceeds thirty percent (30%).

Section 4.13. Except as the Association may otherwise agree, by July 1, 1997, KNEHC shall terminate all special discounts for household use of power and heat resources.

ARTICLE V

Effective Date; Termination; Cancellation and Suspension

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

Section 5.02. (a) This Agreement and all obligations of the Association and of KNEHC thereunder shall terminate on the earlier of the following two dates:

- (i) the date on which the Development Credit Agreement shall terminate in accordance with its terms; or
- (ii) the date twenty years after the date of this Agreement.

(b) If the Development Credit Agreement terminates in accordance with its terms before the date specified in paragraph (a) (ii) of this Section, the Association shall promptly notify KNEHC of this event.

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

ARTICLE VI

Miscellaneous Provisions

Section 6.01. Any notice or request required or permitted to be given or made under this Agreement and any agreement between the parties contemplated by this Agreement shall be in writing. Such notice or request shall be deemed to have been duly given or made when it shall be delivered by hand or by mail, telegram, cable, telex or radiogram to the party to which it is required or permitted to be given or made at such party's address hereinafter specified or at such other address as such party shall have designated by notice to the party giving such notice or making such request. The addresses so specified are:

For the Association:

International Development Association
1818 H Street, N.W.
Washington, D.C. 20433
United States of America

Cable address:

INDEVAS
Washington, D.C.

Telex:

197688 (TRT),
248423 (RCA),
64145 (WUI) or
82987 (FTCC)

For KNEHC:

Kyrgyz National Energy
Holding Company
326, Jibek Jolu
Bishkek 720070
Kyrgyz Republic

Telex:

245128 FIDER

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

Section 6.03. This Agreement may be executed in several counterparts, each of which shall be an original, and all collectively but one instrument.

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

INTERNATIONAL DEVELOPMENT ASSOCIATION

By /s/ Yukon Huang
Acting Regional Vice President
Europe and Central Asia

KYRGYZ NATIONAL ENERGY
HOLDING COMPANY

By /s/ Almas T. Chukin
Authorized Representative

SCHEDULE 1

Procurement and Consultants' Services

Section I: Procurement of Goods

Part A: General

Goods shall be procured in accordance with the provisions of Section I of the "Guidelines for Procurement under IBRD Loans and IDA Credits" published by the Bank in January 1995 (the Guidelines) and the following provisions of this Section, as applicable.

Part B: International Competitive Bidding

1. Except as otherwise provided in Part C of this Section, goods shall be procured under contracts awarded in accordance with the provisions of Section II of the Guidelines and paragraph 5 of Appendix 1 thereto.

2. Preference for domestically manufactured goods

The provisions of paragraphs 2.54 and 2.55 of the Guidelines and Appendix 2 thereto shall apply to goods manufactured in the territory of the Borrower.

Part C: Other Procurement Procedures

International Shopping

Goods estimated to cost the equivalent of \$50,000 or less per contract, up to an aggregate amount not to exceed the equivalent of

\$400,000, may be procured under contracts awarded on the basis of international shopping procedures in accordance with the provisions of paragraphs 3.5 and 3.6 of the Guidelines.

Part D: Review by the Association of Procurement Decisions

1. Procurement Planning

Prior to the issuance of any invitations to bid for contracts, the proposed procurement plan for the Project shall be furnished to the Association for its review and approval, in accordance with the provisions of paragraph 1 of Appendix 1 to the Guidelines. Procurement of all goods shall be undertaken in accordance with such procurement plan as shall have been approved by the Association, and with the provisions of said paragraph 1.

2. Prior Review

With respect to all contracts awarded under Parts B and C of this Schedule, the procedures set forth in paragraphs 2 and 3 of Appendix 1 to the Guidelines shall apply.

Section II. Employment of Consultants

1. Consultants' services shall be procured under contracts awarded in accordance with the provisions of the "Guidelines for the Use of Consultants by the World Bank Borrowers and by the World Bank as Executing Agency" published by the Bank in August 1981 (the Consultant Guidelines). For complex, time-based assignments, such contracts shall be based on the standard form of contract for consultants' services issued by the Association, with such modifications thereto as shall have been agreed by the Association. Where no relevant standard contract documents have been issued by the Association, other standard forms acceptable to the Association shall be used.

2. Notwithstanding the provisions of paragraph 1 of this Section, the provisions of the Consultants Guidelines requiring prior Association review or approval of budgets, short lists, selection procedures, letters of invitation, proposals, evaluation reports and contracts, shall not apply to: (a) contracts for the employment of consulting firms estimated to cost less than \$100,000 equivalent each; or (b) contracts for the employment of individual consultants estimated to cost less than \$50,000 equivalent each. However, said exceptions to prior Association review shall not apply to: (a) the terms of reference for such contracts; (b) single-source selection of consulting firms; (c) assignment of critical nature, as reasonably determined by the Association; (d) amendments to contracts for the employment of consulting firms raising the contract value to \$100,000 equivalent or above; or (e) amendments to contracts for the employment of individual consultants raising the contract value to \$50,000 equivalent or above.

