Loan Agreement

(District Heating Project)

between

INTERNATIONAL BANK FOR RECONSTRUCTION
AND DEVELOPMENT

and

HRVATSKA ELEKTROPRIVREDA D.D.

Dated September 11, 2006
LOAN AGREEMENT

Agreement dated September 11, 2006, between INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT (“Bank”) and HRVATSKA ELEKTROPRIVREDA D.D. (“Borrower”) (“Loan Agreement”). The Borrower and the Bank hereby agree as follows:

ARTICLE I - GENERAL CONDITIONS; DEFINITIONS

1.01. The General Conditions (as defined in the Appendix to this Agreement) constitute an integral part of this Agreement.

1.02. Unless the context requires otherwise, the capitalized terms used in the Loan Agreement have the meanings ascribed to them in the General Conditions.

ARTICLE II - LOAN

2.01. The Bank agrees to lend to the Borrower, on the terms and conditions set forth or referred to in this Agreement, the amount of twenty-four million Euro (EUR 24,000,000) (“Loan”), to assist in financing the project described in Schedule 1 to this Agreement (“Project”).

2.02. The Borrower may withdraw the proceeds of the Loan in accordance with Section IV of Schedule 2 to this Agreement.

2.03. The Commitment Charge payable by the Borrower shall be equal to three-fourths of one percent (3/4 of 1%) per annum on the Unwithdrawn Loan Balance, subject to any waiver of a portion of such charge as may be determined by the Bank from time to time.

2.04. The Front-end Fee payable by the Borrower shall be equal to one percent (1.0%) of the Loan amount, subject to any waiver of a portion of such fee as may be determined by the Bank from time to time.

2.05. The interest payable by the Borrower for each Interest Period shall be at a rate equal to LIBOR for the Loan Currency plus the Variable Spread, subject to any waiver of a portion of such interest as may be determined by the Bank from time to time.

2.06. The Payment Dates are March 15 and September 15 in each year.
2.07. The principal amount of the Loan shall be repaid in accordance with the amortization schedule set forth in Schedule 3 to this Agreement.

**ARTICLE III - PROJECT**

3.01. The Borrower declares its commitment to the objectives of the Project. To this end, the Borrower shall cause the Project Implementing Entity to carry out the Project in accordance with the provisions of Article V of the General Conditions.

3.02. Without limitation upon the provisions of Section 3.01 of this Agreement, and except as the Borrower and the Bank shall otherwise agree, the Borrower shall ensure that the Project is carried out in accordance with the provisions of Schedule 2 to this Agreement.

**ARTICLE IV - REMEDIES OF THE BANK**

4.01. The Additional Event of Suspension consists of the following:

(a) The Project Implementing Entity’s Legislation has been amended, suspended, abrogated, repealed or waived so as to affect materially and adversely the ability of the Project Implementing Entity to perform any of its obligations under the Project Agreement.

4.02. The Additional Event of Acceleration consists of the following:

(a) The event specified in paragraph (a) of Section 4.01 of this Agreement occurs.

**ARTICLE V - EFFECTIVENESS**

5.01. The Additional Conditions of Effectiveness consist of the following:

(a) The Subsidiary Agreement has been executed on behalf of the Borrower and the Project Implementing Entity.

(b) The Subsidiary Guarantee Agreement has been executed between the Ministry of Finance, on behalf of the Guarantor, and the Borrower.

5.02. The Additional Legal Matters consist of the following:

(a) The Subsidiary Agreement has been duly authorized or ratified by the Borrower and the Project Implementing Entity and is legally binding upon the Borrower and the Project Implementing Entity in accordance with its terms.
(b) The Subsidiary Guarantee Agreement has been duly authorized or ratified by the Guarantor and the Borrower and is legally binding upon the Guarantor and the Borrower in accordance with its terms.

5.03. The Effectiveness Deadline is the date ninety (90) days after the date of this Agreement.

ARTICLE VI - REPRESENTATIVE; ADDRESSES

6.01. The Borrower’s Representative is the President of the Management Board.

6.02. The Borrower’s Address is:

Hrvatska Elektroprivreda d.d.
Ulica Grada Vukovara 37
Zagreb 10000
Republic of Croatia

Facsimile:

(385-1) 6170-439
(385-1) 6322-651

6.03. The Bank’s Address is:

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

Cable address: INTBAFRAD
Telex: 248423(MCI) or 64145(MCI)
Facsimile: 1-202-477-6391
AGREED at Zagreb, Republic of Croatia, as of the day and year first above written.

INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT

By: /s/ Anand K. Seth
Authorized Representative

HRVATSKA ELEKTROPRIVREDA D.D.

By: /s/ Ivan Mravak
Authorized Representative
SCHEDULE 1

Project Description

The objective of the Project is to promote efficient provision of district heating services by the Project Implementing Entity.

The Project consists of the following parts:

A. Infrastructure Rehabilitation

1. Network rehabilitation, including replacement of a dual pipe trench, transmission pipes, and distribution pipes in the City of Zagreb.

2. Network rehabilitation, including replacement of distribution pipes that are in poor condition and connection of customers to the main Combined Heat and Power Plant, and rehabilitation of selected heating sub-stations in the City of Osijek.

B. Consultancy Services

1. Development and implementation of a Demand Side Management program.

2. Completion of two (2) customer surveys in the Cities of Zagreb and Osijek.

3. Preparation of bidding documents for the Project.

4. Construction supervision under the Project.

5. Preparation of annual audits of the financial statements of the Project and of the Project Implementing Entity.
SCHEDULE 2

Project Execution

Section I. Subsidiary Financing; Institutional and Other Arrangements

A. Subsidiary Agreement

1. To facilitate the carrying out of the Project by the Project Implementing Entity, the Borrower shall make the proceeds of the Loan available to the Project Implementing Entity under a separate subsidiary agreement between the Borrower and the Project Implementing Entity (“Subsidiary Agreement”), under terms and conditions approved by the Bank, which shall include the following: (a) on-lent proceeds of the Loan to be denominated in Euro; (b) repayment of the proceeds of the Loan over a period of fifteen (15) years, inclusive of a grace period of five (5) years; (c) payment of interest on the principal amount of the Loan withdrawn and outstanding from time to time at the rate payable by the Borrower pursuant to Section 2.05 of this Agreement; and (d) payment of a commitment charge on the Unwithdrawn Balance at the rate payable by the Borrower pursuant to Section 2.03 of this Agreement.

2. The Borrower shall exercise its rights under the Subsidiary Agreement in such manner as to protect the interests of the Borrower and the Bank and to accomplish the purposes of the Loan. Except as the Bank shall otherwise agree, the Borrower shall not assign, amend, arrogate or waive the Subsidiary Agreement or any of its provisions.

B. Other covenants

1. The Borrower, jointly with the Project Implementing Entity, shall maintain at all times during Project implementation, the Project Implementation Unit, with terms of reference and resources satisfactory to the Bank, and competent staff in adequate numbers.

2. The Borrower shall, and shall cause the Project Implementing Entity, to implement the Project in accordance with the provisions of the Environmental Management Plan and of the Land Acquisition Framework, if applicable, both satisfactory to the Bank, and shall not amend, suspend or abrogate any of their provisions without the prior agreement of the Bank.

Section II. Project Monitoring, Reporting, Evaluation

A. Project Reports

1. The Borrower shall, and shall cause the Project Implementing Entity, to monitor and evaluate the progress of the Project and prepare Project Reports, commencing from December 31, 2006, in accordance with the provisions of Section 5.08 of the General
Conditions and on the basis of the indicators agreed with the Bank. Each Project Report shall cover the period of one (1) calendar semester, and shall be furnished to the Bank not later than one (1) month after the end of the period covered by such report.

2. For purposes of Section 5.08 (c) of the General Conditions, the report on the execution of the Project and related plan required pursuant to that Section shall be furnished to the Bank and to the Guarantor not later than June 30, 2010.

B. Financial Management, Financial Reports and Audits

1. The Borrower shall maintain or cause to be maintained a financial management system in accordance with the provisions of Section 5.09 of the General Conditions.

2. Without limitation on the provisions of Part A of this Section, the Borrower shall prepare and furnish to the Bank and to the Guarantor not later than one month (1) after the end of each calendar quarter, interim un-audited financial reports for the Project covering the respective quarter, in form and substance satisfactory to the Bank.

3. The Borrower shall have its Financial Statements audited in accordance with the provisions of Section 5.09 (b) of the General Conditions. Each audit of the Financial Statements shall cover the period of one (1) fiscal year of the Borrower, commencing with the fiscal year in which the Project became effective, and shall be adequate to reflect the operations and financial condition of the Borrower and to register separately the operations, resources and expenditures of the Borrower related to the Project. The audited Financial Statements for each such period shall be furnished to the Bank not later than six (6) months after the end of such period.

Section III. Procurement

A. General

1. Goods and Works. Except as the Bank shall otherwise agree, all goods, works and services (other than consulting services) required for the Project and to be financed out of the proceeds of the Loan shall be procured in accordance with the requirements set forth or referred to in Section I of the Procurement Guidelines, and with the provisions of this Section.

2. Definitions. The capitalized terms used below in this Section to describe particular procurement methods or methods of review by the Bank of particular contracts refer to the corresponding method described in the Procurement Guidelines.
B. Particular Methods of Procurement of Goods and Works

1. International Competitive Bidding. Except as otherwise provided in paragraph 2 below, goods and works shall be procured under contracts awarded on the basis of International Competitive Bidding. The provisions of paragraphs 2.55 and 2.56 of the Procurement Guidelines, providing for domestic preference in the evaluation of bids, shall apply to goods manufactured in the territory of the Borrower.

2. Other Methods of Procurement of Goods and Works. The following table specifies the methods of procurement, other than International Competitive Bidding, which may be used for goods and works. The Procurement Plan shall specify the circumstances under which such methods may be used.

<table>
<thead>
<tr>
<th>Procurement Method</th>
</tr>
</thead>
<tbody>
<tr>
<td>(a) National Competitive Bidding (subject to additional provisions set forth in this Section)</td>
</tr>
<tr>
<td>(b) Shopping</td>
</tr>
<tr>
<td>(c) Direct Contracting</td>
</tr>
</tbody>
</table>

(a) National Competitive Bidding. Works estimated to cost less than EUR 4,200,000 equivalent per contract, and goods estimated to cost less than EUR 800,000 equivalent per contract, may be procured under contracts awarded on the basis of National Competitive Bidding and the following additional provisions set forth in (i) through (viii) of this paragraph. The Bank may, upon notice to the Borrower, increase the above threshold for goods to be procured on the basis of the National Competitive Bidding.

(i) Procedures

The public bidding method shall apply to all contracts. Invitations to bid shall be advertised in the Guarantor’s Official Gazette (Narodne Novine) and in at least one (1) widely circulated national daily newspaper or at the Borrower’s website, allowing a minimum of thirty (30) days for the preparation and submission of bids.

(ii) Assessment of Bidders’ Qualifications

When pre-qualification shall be required for large or complex works contracts, invitations to pre-qualify for bidding shall be
advertised in the Guarantor’s Official Gazette (Narodne Novine) and at least (1) one widely circulated national daily newspaper a minimum of thirty (30) days prior to the deadline for the submission of pre-qualification applications. Minimum experience, technical and financial requirements shall be explicitly stated in the pre-qualification documents, which shall be determined by a ‘pass/fail’ method, not through the use of a merit point system. Where pre-qualification is not used, the qualifications of the bidder who is recommended for award of contract shall be assessed by post-qualification, applying minimum experience, technical and financial requirements which shall be explicitly stated in the bidding documents.

(iii) Participation of Government-owned Enterprises

Government-owned enterprises located and operating on the Guarantor’s territory shall be eligible to participate in bidding only if they can establish, to the Bank’s satisfaction, that they are legally and financially autonomous, operate under commercial laws and are not a dependent agency of the Guarantor’s Government. Said enterprises shall be subject to the same bid and performance security requirements as other bidders.

(iv) Bidding Documents

Project Implementing Entity acting as procuring entity shall use the appropriate standard bidding documents for the procurement of goods, works or services, as defined in paragraph 1.1 of the Guidelines, which shall contain draft contract and conditions of contract acceptable to the Bank.

(v) Bid Submission, Opening and Evaluation

(1) Bids shall be submitted in a single envelope containing the bidder’s qualification information, technical and price bids, which shall be opened simultaneously at the public bid opening.

(2) Bids shall be opened in public, immediately after the deadline for submission of bids. The name of the bidder, the total amount of each bid and any discounts offered shall be read aloud and
recorded in the minutes of the public bid opening.

(3) The evaluation of bids shall be done in strict adherence to the monetarily quantifiable criteria specified in the bidding documents and a merit point system shall not be used.

(4) Extension of bid validity shall be allowed once only for not more than thirty (30) days. No further extensions should be granted without the prior approval of the Bank.

(5) Contracts shall be awarded to qualified bidders having submitted the lowest evaluated substantially responsive bid.

(6) No preference shall apply under National Competitive Bidding.

(vi) Price Adjustment

Works contracts of long duration (e.g. more than eighteen (18) months) shall contain an appropriate price adjustment clause.

(vii) Rejection of All Bids

(1) All bids shall not be rejected and new bids solicited without the Bank’s prior written concurrence.

(2) When the number of bids received is less than two (2), re-bidding shall not be carried out without the Bank’s prior concurrence.

(viii) Securities

Bid securities should not exceed two percent (2%) of the estimated cost of the contract; and performance securities – not more than ten percent (10%). No advance shall be made to contractors without a suitable advance payment security. The wording of all such securities shall be included into the bidding documents and shall be acceptable to the Bank.
(b) **Shopping.** Goods and works estimated to cost less than EUR 60,000 equivalent per contract, may be procured under contracts awarded on the basis of Shopping procedures in accordance with the provisions of paragraphs 3.1 and 3.5 of the Guidelines.

(c) **Direct Contracting.** Goods and works which the Bank agrees meet the requirements for Direct Contracting may be procured in accordance with the provisions of paragraph 3.6 of the Guidelines and such contracts shall be included in the Procurement Plan or its updates agreed with the Bank.

**C. Review by the Bank of Procurement Decisions**

The Procurement Plan shall set forth those contracts which shall be subject to the Bank’s Prior Review. All other contracts shall be subject to Post Review by the Bank.

**Section IV. Withdrawal of Loan Proceeds**

**A. General**

1. The Borrower may withdraw the proceeds of the Loan in accordance with the provisions of this Section and such additional instructions as the Bank shall specify by notice to the Borrower to finance Eligible Expenditures as set forth in the table in paragraph 2 below.

2. The following table specifies the categories of Eligible Expenditures that may be financed out of the proceeds of the Loan (“Category”), the allocation of the amounts of the Loan to each Category, and the percentage of expenditures to be financed for Eligible Expenditures in each Category.

<table>
<thead>
<tr>
<th>Category</th>
<th>Amount of the Loan Allocated (expressed in EUR)</th>
<th>Percentage of Expenditures to be Financed</th>
</tr>
</thead>
<tbody>
<tr>
<td>(1) Works for Part A.1 of the Project</td>
<td>5,270,000</td>
<td>100%</td>
</tr>
<tr>
<td>(2) Goods for Part A.1 of the Project</td>
<td>12,600,000</td>
<td>100%</td>
</tr>
<tr>
<td>(3) Works for Part A.2 of the Project</td>
<td>2,600,000</td>
<td>100%</td>
</tr>
<tr>
<td>(4) Goods for Part A.2 of the Project</td>
<td>3,470,000</td>
<td>100%</td>
</tr>
<tr>
<td>Category</td>
<td>Amount of the Loan Allocated (expressed in EUR)</td>
<td>Percentage of Expenditures to be Financed</td>
</tr>
<tr>
<td>------------------</td>
<td>-----------------------------------------------</td>
<td>------------------------------------------</td>
</tr>
<tr>
<td>(5) Front-end Fee</td>
<td>60,000</td>
<td>Amount payable pursuant to Section 2.04 of this Agreement in accordance with Section 2.07 (b) of the General Conditions</td>
</tr>
<tr>
<td>TOTAL AMOUNT</td>
<td>24,000,000</td>
<td></td>
</tr>
</tbody>
</table>

**B. Withdrawal Conditions; Withdrawal Period**

1. Notwithstanding the provisions of Part A of this Section, no withdrawal shall be made: (a) for payments made prior to the date of this Agreement, except that withdrawals up to an aggregate amount not to exceed EUR 2,400,000 equivalent may be made for payments made prior to this date but on or after March 20, 2006, for Eligible Expenditures under all Categories, provided that the disbursement condition for Categories (1) and (2) set forth in paragraph (b) of this Section B.1 has been complied with; (b) for payments under Categories (1) and (2) unless the Borrower has furnished to the Bank satisfactory evidence that a contract for delivery of heat between the City of Zagreb and the Project Implementing Entity has been duly executed.

2. The Closing Date is June 30, 2010.

**Section V. Other Undertakings**

1. (a) Except as the Bank shall otherwise agree, the Borrower shall not incur any debt, unless the net revenues of the Borrower for the fiscal year immediately preceding the date of such incurrence or for a later twelve-month period ended prior to the date of such incurrence, whichever is the greater, shall be at least 1.2 times the estimated maximum debt service requirements of the Borrower for any succeeding fiscal year on all debt of the Borrower, including the debt to be incurred.

   (b) For the purposes of this Section:

      (i) The term "debt" means any indebtedness of the Borrower maturing by its terms more than one (1) 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 adjusted to take account of the Borrower's tariffs in effect at the time of the incurrence of debt even though they were not in effect during the twelve-month period to which such revenues relate 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) Whenever for the purposes of this Section it shall be necessary to value, in terms of the currency of the Guarantor, debt payable in another currency, such valuation shall be made on the basis of the prevailing lawful rate of exchange at which such other currency is, at the time of such valuation, obtainable for the purposes of servicing such debt, or in the absence of such rate, on the basis of a rate of exchange acceptable to the Bank.

2. The Borrower shall:
(a) by March 31 of each year during Project implementation, review with the Bank its financial performance for the preceding year and the financial forecasts for the next two (2) years;

(b) jointly with the Project Implementing Entity, by March 31 of each year during Project implementation, review with the Bank the financial performance of the Project Implementing Entity for the preceding year and the financial forecasts for the next two (2) years; and

(c) take appropriate actions required for the Project Implementing Entity to meet its financial obligations under the Project Agreement, including proposing to HERA the adjustment of the levels and structure of tariffs for district heating which would allow the Project Implementing Entity, under conditions of efficient operation at reasonable levels of capacity utilization, to cover: its operating costs including depreciation; debt service payments, including debt service payments on the Loan; reduction of payment arrears, and provision of internally generated funds for financing of investments under the Project.

3. Not later than October 31, 2006, the Borrower shall furnish to the Bank an agreed schedule to eliminate the Project Implementing Entity’s arrears to the Borrower with respect to the purchase of heat and steam, and shall thereafter implement said schedule, in line with the Guarantor’s applicable tariff regulations and in a manner satisfactory to the Bank.
### SCHEDULE 3

Amortization Schedule

<table>
<thead>
<tr>
<th>Principal Payment Date</th>
<th>Principal Amount of the Loan Payable (Expressed in Euro)</th>
</tr>
</thead>
<tbody>
<tr>
<td>On each March 15 and September 15 beginning March 15, 2012 through September 15, 2021</td>
<td>1,200,000.00</td>
</tr>
</tbody>
</table>
APPENDIX

Definitions

1. “Category” means a category set forth in the table in Section IV of Schedule 2 to this Agreement.

2. “Conclusion of the Government of the Republic of Croatia Class No. 310-02/06-02/05, Reg. No. 5030122-06-01” means the Conclusion of the Government of the Republic of Croatia adopted on May 5, 2006, (No. 310-02/06-02/05) which sets forth a framework (2007-2010) for development of the district heating sector in the Republic of Croatia, to be implemented by MOELE and supported through the state budget, including measures for improving sustainability of district heating companies, supporting low-income and vulnerable groups under the existing social assistance program, and introducing Demand Side Management.


4. “Demand Side Management” means a system which allows consumers to regulate heat consumption and provides for billing the end-users of district heating for actual consumption, as determined through installment of equipment for measuring district heating consumption in households.

5. “Environmental Management Plan” means a plan adopted by the Borrower, describing the environmental mitigation, monitoring and institutional measures for the Project.


8. “HERA” means Hrvatska Energetska Regulatorna Agencija (the Croatian Energy Regulatory Agency) established pursuant to the Law on Energy (177/2004), or any legal successor thereto.

9. “Land Acquisition Framework” means a document “Framework for Real Estate Acquisition and Establishment of the Right of Servitude” adopted by the Borrower and the Project Implementing Entity which sets forth policies and procedures, in accordance with the Guarantor’s applicable laws and regulations,
to be followed in case of land acquisition for carrying out of the Project activities.

10. “MOELE” means the Guarantor’s Ministry of Economy, Labor and Entrepreneurship, or any legal successor thereto.


12. “Procurement Plan” means the Borrower’s procurement plan for the Project, dated May 10, 2006, and referred to in paragraph 1.16 of the Procurement Guidelines and paragraph 1.24 of the Consultant Guidelines, as the same shall be updated from time to time in accordance with the provisions of said paragraphs.


14. “Subsidiary Agreement” means the agreement referred to in Section I.A.1 of Schedule 2 to this Agreement pursuant to which the Borrower shall make the proceeds of the Loan available to the Project Implementing Entity.

15. “Subsidiary Guarantee Agreement” means an agreement to be entered into between the Ministry of Finance and the Borrower which shall set forth the terms of providing a guarantee for the Loan by the Guarantor.